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HISTORY AND PRINCIPLES OF
BANKS AND BANKING

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HISTORY AND PRINCIPLES
OF
BANKS AND BANKING

BY

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"THE HISTORY OF A BANKING HOUSE"

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PREFACE TO NEW EDITION.

THE original edition stated that the purport of the book was to give an outline of the growth of banking in this country.

So many changes have occurred in our system within the last seven years that it has been found necessary, not only to revise, but also to considerably enlarge, the present volume. The most prominent features during that period are the amalgamation of various banking firms, the multiplication of branches, and, finally, the enormous growth of deposits. For example, in 1896 there were 101 private and 109 joint-stock banks in existence, which have now been reduced by amalgamation to 42 and 64 respectively.

There has been a great increase in the number of branches, as follows :—

BANKING OFFICES, UNITED KINGDOM.

1894	.	.	.	.	.	.	.	.	.	3,889
1902	.	.	.	.	.	.	.	.	.	6,672

The growth of deposits illustrates somewhat the prosperity of the country :—

									£
1896	.	.	.	.	.	.	.	.	798,000,000
1902	.	.	.	.	.	.	.	.	1,525,000,000

The figures for 1896 include an estimated amount of

private bank deposits; but those for 1902 are from actual returns. On this basis we have an increase of £727,000,000, or about £100,000,000 per annum.

The new chapters on "The Management of Deposits" and "Banks and the Stock Exchange" have been added in order to give a brief outline of the practice of banking with respect to surplus funds. It would be impossible in a small manual to give details with respect to all the transactions which form the daily routine of our great banking institutions.

The author hopes that the book may be useful to candidates for the Examinations of the Institute of Bankers, and for this purpose some of the questions given have been appended.

PREFACE TO FIRST EDITION.

THIS small volume consists of a series of notes on the growth and development of banking in this country. The author has endeavoured to show how the deposit of money in a bank has developed into a complex system of finance, and also how capital, wielding an immense power in the present day, is largely under the management and control of our great banking institutions. The study of banking is of great importance when we consider how dependent the commercial world is upon the existence of a perfectly sound system. To understand the why and wherefore of credit, which forms the basis of banking, is an essential study for those who have adopted it as their profession.

As to the sequence of the work it has been thought desirable, in the first place, to give a short sketch of early banking in this country, and then as an outcome of the expansion of trade to show its connection with commerce. In the early history of banking the subject of the currency was the most prominent feature, and therefore it has been treated separately.

The Bank of England occupies such an important position that an account of the rise and progress of that institution is given. The subsequent chapters consist of a series of notes on the history of English, Scotch and Irish Banks.

The connection between commercial crises and banking is of such an intimate character that the leading incidents of every important crisis have been given.

Modern banking is so dependent upon the rate of interest which determines the profits of banks that it has been considered desirable to give a somewhat lengthened account of the causes of fluctuations in the value of money.

The concluding chapters are devoted to incidents of modern practice, such as cheques, bills of exchange and the opening of branch offices.

The author hopes that the notes may be of some value to those candidates who are preparing for the Institute of Bankers' Examinations.

Reference is made to such standard works as Bagehot's *Lombard Street*, Professor Jevons' *Money and Investigations of Currency and Finance*, Professor Marshall's *Principles of Economics*, and *Notes on Banking* by Mr. Palgrave, and the author trusts that his notes may serve as an introduction to such excellent manuals of finance. The yearly volumes of the Institute of Bankers have also been of great service, as they form almost an encyclopædia of banking.

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BANKS AND BANKING.

CHAPTER I.

INTRODUCTION.

THE study of banking is of great importance, since the commercial prosperity of this country is largely dependent upon the stability of our banking system.

We might almost say that the entire capital of the country finds its way into banks in order to be utilised for the benefit of the community. For example, a manufacturer, by the aid of borrowed capital obtained from such institutions, is able to produce commodities at a cheaper rate, and thus benefit society at large. It is a known axiom of political economy that an increase of production is a cheapening process. Our modern system of banking has materially increased the prosperity of this country, since no country in the world has the same monetary facilities as we have for carrying on trade. Abolish our present advantages, and we should find it difficult to compete with other countries; in fact, English commerce would be heavily handicapped.

We must endeavour to ascertain why banking became such an important factor in everyday life.

The answer is a simple one; when people accumulated capital a need was felt for a place where it could be kept in safety; such places were designated banks, and they became the storehouses of capital.

Some medium was required by means of which capital could be transferred or exchanged; we find that from an early period the precious metals were utilised for the purpose of transferring wealth from one person to another. There would be some risk in hoarding gold and silver, consequently, in course of time the precious metals, in the form of coin, were deposited in banks.

The study of banking is, therefore, intimately associated with the growth of capital and the circulating medium.

The subject of the currency is an important one, since not only gold and silver formed the basis of exchange, but from an early period another medium for the transfer of capital or debt, *viz.*, bank notes, came into existence. Now, if a paper currency is introduced into a country, the question arises as to the amount issued, and also what safeguards are necessary in order that bank notes shall *always* be convertible into gold on demand. In this country a definite amount was fixed, and it so happened that the limit in many respects was a good one.

Unfortunately there is no universal standard with regard to the metallic circulation. In this country we have a standard of value in the form of gold, with a subsidiary coinage of silver and copper. This is advantageous, but other countries have adopted a silver currency as a legal tender, and when we have to settle differences of trade with such countries, a disturbing element interferes with the transaction. Thus, capital and currency are most important factors in the study of banking.

We have, however, another important one, *viz.*, credit, because upon this edifice our system of banking is built up. Credit is the basis for our commercial transactions; one person takes a cheque from another, since he believes that the drawer has sufficient capital at his banker's to pay the cheque on presentation.

This system is comparatively of recent origin, and it has been the means of economising the use of the precious metals. If payments of debts by means of cheques were abolished, a large amount of gold would be required; this would mean capital in an unremunerative form.

The growth of capital in this country is the principal cause of the rise of banking.

We had, at an early date, merchants who at first were traders and bankers, but subsequently found that, with the rapid accumulation of capital in their hands, it was impossible to carry on two distinct transactions, so that the former business was abandoned, and banking became their sole profession.

In consequence of the growth of trade more banking facilities were required; and then a great institution was formed, which, in course of time, became a model for the whole world. This institution was the Bank of England, and its history is really an account of the rapid growth of English trade, as well as illustrating the accumulation of wealth in this country.

Capital finds its way into banks, but its movements are largely dependent upon the state of credit. A bank is, therefore, a place where capital is deposited either for safe custody or to be utilised for certain purposes.

It may also be left by a depositor as a reserve for present or future requirements; we can easily understand how it may happen that a sudden withdrawal of deposits takes place.

A declaration of war, a rebellion, or a series of failures, might seriously imperil the existence of our banking institutions.

We have, in fact, three important subjects in the study of banking, *viz.*, capital, currency and credit.

As the trade of our country expanded, more banking

facilities were required, and then we find that Joint-Stock Banks came into existence.

These institutions had at first to encounter great opposition from their rivals; but, in course of time, they became the most important factors in our banking system. It is therefore necessary to give an account of the private banks, the Bank of England and the Joint-Stock Banks, in order to follow the growth of banking.

Again, when our foreign trade increased, it was necessary to have institutions which could make an especial study of the needs of our colonies and foreign countries; consequently, banks were formed to carry on this particular business.

For example, Australian Banks advance capital against the staple article of the country, *viz.*, wool; whereas banks which transact business with Argentina confine themselves principally to dealings in wheat—the chief produce of the country.

The functions of a bank consist in the borrowing and lending of capital; the difference between the amount paid to the lender and that paid by a borrower constitutes part of the profits earned in the management of capital.

There is also an additional amount received through the employment of capital, left by the customer without interest, as a kind of reserve, or in consideration of services rendered by the bank.

With the exception of a small portion, kept as a cash reserve, the whole of the capital lodged in banks is lent at interest, and constitutes the profits, which fluctuate with the supply and demand for capital.

It will therefore be necessary to consider what constitutes the demand, and what are the influences which govern the supply.

There are also fluctuations caused by movements of gold, because that metal is the basis upon which the price of all commodities is fixed.

In this country we have what is known as the one reserve system, *viz.*, one bank practically holding the cash reserve. Now, as this reserve is increased or diminished, the value or price of commodities will rise or fall. We shall also notice movements of capital due to the issue of bank notes which are repayable in gold on demand.

Our gigantic system of credit is based upon a small cash reserve, which is seen from the following gold reserves of other countries :—

	1901.
England.	33,800,000
France	97,960,000
Germany	45,570,000

We see, therefore, that England, with enormous trade transactions throughout the world, has a small metallic reserve compared with other countries.

Of course, capital lying idle is unproductive ; but, at the same time, there are dangers connected with a small cash reserve.

Gold and silver must be bought like other commodities, and when stored in banks represent capital in reserve, so that, as our banking system is effected by means of a comparatively small amount of the precious metals, the capital of the country is economised. Whenever there exists a good system of banking, we should naturally expect to find a prosperous state of affairs.

English banking is comparatively modern, because two hundred and twenty years ago the banker of that day was simply a goldsmith, although he also advanced money upon plate, jewellery, etc. Again, the Bank of England was not in existence, the date of its charter being 27th

July, 1694 ; and, lastly, joint-stock banking was also unknown, although it was not declared illegal until the renewal of the Bank Charter in 1708.

At an earlier period the business of money lending was carried on by the Jews, who transacted business at very high rates of interest, although a law had been passed in the reign of Edward the Confessor prohibiting usury.

However, we find that in the year 1199 the rate of interest was fixed by law at 10 per cent., and this appears to have been the rate until the reign of Henry VIII. It is stated that the Jews at Oxford, during the reigns of Henry III. and Edward I., were in the habit of extracting 45 per cent. from the students. The matter was taken up by the legislature, and Henry III. granted a charter by which they were only to receive interest at the rate of 2d. in the £ weekly. Money so obtained from the Jews did not benefit the trade of the country, but only of individuals who were in pecuniary difficulties.

The Jews were thoroughly hated for the manner in which they transacted business, and consequently were expelled from England in the year 1290, and not readmitted until the time of Oliver Cromwell.

The Lombards were also money lenders, having settled in this country at an early period from Genoa, Venice, Lucca and Florence. They lent large sums of money to different governments, for which, like the Jews, they charged an exorbitant rate of interest. Edward III. borrowed 5,000 marks from them, for which he paid 7,000 marks.

Besides the Jews and Lombards there was another class who were originally dealers in gold and silver bullion, but who became subsequently bankers. These men were called goldsmiths, and possessed considerable wealth. Mr. Price, in his *Handbook of London Bankers*,

gives a very interesting account of these early goldsmiths and money lenders.

Amongst the early goldsmiths we have Otto, in the reign of William I., and later Henry Fitz Alwin Fitz Leofstane, who was Lord Mayor of London for twenty-four years, from 1189 to 1213. In the reign of Henry III. three goldsmiths are mentioned, *viz.*, Thomas de Frowick, Warden of the Goldsmiths Company in 1270, and Alderman of Cheap Ward in 1279; William de Gloucester, Keeper of the Dies in 1255; and William, the King's Goldsmith, Master of the Mint in 1258. The names of seven goldsmiths are recorded between the years 1327 and 1377.

In 1566 the Court books of the Goldsmiths Company show that out of 107 no less than 76 of them resided in "Chepe"; the remaining 31 resided in "Lumberde Street". It was during the Commonwealth that the goldsmiths began to assume the character of bankers. Many persons left their money with the goldsmiths for safe-keeping, and in return the goldsmiths gave receipts or cash notes for the same, payable on demand. These receipts passed from hand to hand, and were called goldsmiths' notes. At a later period the goldsmiths deposited their money with the Government.

There was a feeling of insecurity during the Civil War, so that money kept in large iron chests was removed to places of safety; the chief investments at that time for capital being land and cattle.

It is stated in the Verney Memoirs that on the death of Lady Verney in 1641 she directs by her will that certain sums of money should be taken from a red box and distributed amongst her relatives.

During the same period the capital of many noblemen consisted principally of live stock on their estates.

Charles II., being in want of money, closed the Ex-

chequer, and all payments to bankers who had deposited money in that place were suspended. The goldsmiths had at that time £1,328,526 on deposit, and the loss of this large sum naturally brought ruin upon them and their customers. It was not until five years after that the king caused *letters patent* to be granted to the goldsmiths covenanting to pay 6 per cent. per annum on the amount taken from them. but even this was discontinued in 1683.

The number of goldsmiths or bankers that were in existence at the end of the seventeenth century amounted to about 70 or 80, but at the end of another 100 years they had not increased in number. In the year 1801 there were 68 private bankers in London.

Many of the goldsmiths whose names we find recorded in the *Little London Directory* still exist as bankers of the present day. Of these we have Messrs. Hoare & Co., descended from James Hore or Hoare, a goldsmith keeping running cashes at the Golden Bottle in Cheapside, 1677; Messrs. Child & Co., descended from Messrs. Blanchard & Child of "Ye Marygold"; Messrs. Martin & Co., descended from Charles Duncombe and Richard Kent of "Ye Grasshopper," in Lombard Street; and Messrs. Barnett & Co., descended from Humphry Stocks of the "Black Horse" in Lombard Street. but now amalgamated with Lloyds Bank.

The oldest provincial bank was Samuel Smith & Co., of Nottingham, until its amalgamation with the Union Bank of London. This bank was founded in 1688 by Thomas Smith, a mercer in that town; its origin was due to the fact that people from the neighbourhood came to Nottingham on market days and found it desirable to leave their spare capital for safe custody with Thomas Smith, who realised that it could be profitably employed.

and suggested giving interest to the depositor, which, of course, was at once accepted. His grandson, Abel, in 1758, founded the famous house of Messrs. Smith, Payne & Smiths.

The London bankers met with a serious rival in the year 1694, when the Bank of England was founded to carry on the business of banking. This institution, three years later, obtained the exclusive privilege of joint-stock banking. It was enacted "That during the continuance of the said corporation of the Governor and Company of the Bank of England, it shall not be lawful for any body politic or corporate whatsoever erected or to be erected (other than the said Governor and Company of the Bank of England), or for any other persons whatsoever united or to be united in covenant or partnership exceeding the number of six persons in that part of Great Britain called England, to borrow, owe, or take up any sum or sums of money on their bills or notes payable at demand, or at any less time than six months from the borrowing thereof".

Very little is known with respect to the country bankers ; it is supposed that very few existed prior to the American War, but after its termination they increased very rapidly. In the year 1797 there were 270 bankers carrying on business in the country ; unfortunately the country bankers did not possess the wealth of their London brethren, they issued notes, and at times did not have sufficient capital to pay them on demand.

It is stated that "multitudes of miserable shopkeepers in the country, grocers, tailors, drapers, started up like mushrooms and turned bankers. They issued notes and inundated the country with their miserable rags." Burke says that when he came to England in 1750 there were not 12 bankers out of London, but in 1793 there were

nearly 400. This number was reduced by the crisis of 1797 to 270. Of the country bankers now in existence, the names of 61 appeared in the *Post Office London Directory* of 1803.

The London bankers ceased to issue notes at an early period, and found it advantageous to keep Bank of England notes as till money.

The history of English banking to the end of the eighteenth century shows that very little progress had been made, since we could not expect that credit, which is the modern basis of banking, would flourish during times of revolution and war. We might say that the close of this century was the dividing line between the old and the new methods, although the first joint-stock bank was not formed until 1826.

Again, the trade of the country was not sufficiently developed to require the aid of capital; no doubt, if it had increased very rapidly, the monopoly of joint-stock banking given to the Bank of England would have been abolished at an earlier date. The profit of the bankers during this period was derived principally from the issue of bank notes.

CHAPTER II.

BANKING AND COMMERCE.

MODERN banking is so dependent upon the trade of the country that it is important to show the connection before we consider the growth and progress of the various banking institutions.

If trade had not progressed, banking could not have attained its present position; the rapid growth of English commerce in recent years is shown by the enormous increase in the imports and exports, the revenue, and, lastly, by the growth of shipping, which has enabled this country to become the largest carriers in the world.

The abolition of certain restrictive laws enabled the merchant to send his goods to foreign countries without paying excessive duties, and when this country finally adopted the principles of free trade a remarkable stimulus was given to British industries.

In the year 1820 the London merchants petitioned for the removal of restrictive duties. The function of trade is to supply other countries with commodities which they require. When the trade of a country is limited, the economy of production is also retarded; but when the interchange of commodities between different countries is allowed without any restrictions, then such countries will become prosperous. Each country is dependent upon another; for example, one will devote its energies to one industry, say the production of corn; whilst the other will

manufacture machinery for the use of the corn-growing country. We also get a full division of labour, if countries are not restricted by laws which prevent it.

These are the principal arguments in favour of free trade.

Free banking was also required, and consequently in the year 1826 it was enacted that joint-stock companies might be formed for this purpose. Now, it is important to notice how soon the want of more banking facilities was felt, consequent on the rapid growth of English commerce. The amendment of the laws relating to public companies, and known as the Limited Liability Acts, was the cause of the formation of a large number of companies for various purposes. Banking and insurance companies were not allowed to be formed on this principle until the year 1862, when it was enacted that any seven or more persons associated for *any lawful purpose* by subscribing a memorandum of association might constitute themselves a limited or unlimited company.

The abolition of the usury laws was another gain to banking and commerce. The Act of 1833 repealed the usury laws with regard to bills of exchange of three months and under, and four years later this was extended to bills of twelve months and under. In 1839 it was lawful to stipulate for any rate of interest upon which the parties might agree as to all personal contracts, but made an exception as to real securities. The usury laws were abolished entirely in the year 1854.

The tax on receipts was reduced to 1d. in 1853, and in 1854 the stamp duties on bills of exchange were reduced. The payment of custom duties by cheques, instead of by gold and notes, was of some importance to the bankers, because it lessened their gold requirements. We must always remember that the state of trade in this country

is a question of vital importance to the banking institutions. The amount of capital held at the disposal of a banker will vary with the prosperity of the country; he does not create capital, because his resources are obtained from those who deposit the same. We might consider him as a broker between two principals, *viz.*, one deposits capital with him, and he lends it to another whose solvency he guarantees. His position is, therefore, an important one, because he selects the borrower, and whether capital is utilised for a good purpose, or sunk in unprofitable enterprises, is dependent upon his ability to discern between a sound or an unsound borrower. The banker has also to discriminate between the mere speculator and the *bonâ fide* business man.

The rapid growth of trade required plenty of capital, and this could only be obtained through the medium of banks, which have become the great store-houses of capital. All the surplus money, say, of the agricultural districts, finds its way, through the medium of banks, into manufacturing districts where it can be utilised. If an industry is prosperous, then bills of exchange representing transactions in that particular trade will be held by banks as security; if, however, the trade of any industry suddenly becomes bad, then there will be a less number of bills representing it. Capital which has been utilised in that particular business will find its way to some other trade in a more prosperous condition. The advantage of this large floating capital stored up in banks cannot be overestimated, because without it we should not be in such a good position to compete with other nations, or carry on the production of commodities so extensively.

One of the chief reasons why our trade is so great is that this large amount of floating capital can be obtained

from the bankers at a low rate of interest. We can easily understand how the banker is dependent upon the trade of the country for capital to carry on his business. If trade is bad, then there will be little accumulation of capital in banks; but, on the other hand, if good, then it will be increased in such institutions. Sometimes, however, an accumulation of capital may take place, but in consequence of depressed trade there is no demand for it.

Another important point to be noticed in connection with commerce and banking is the mode of carrying on business in the present day. We might say that modern trade is transacted by means of borrowed capital; a successful trader can, as a rule, obtain accommodation from his banker, who will provide him with capital by discounting his bills. Thus, the capital of a trader may only amount to £2,000 or £3,000, yet his transactions would be far in excess of that amount by means of these credit documents.

Modern business transactions are effected either by obtaining advances on the goods bought, or by discounting bills received for goods sold. The difference between the selling price and the cost of production, plus the interest paid to the banker, would constitute the profit. This method of transacting business is comparatively of recent origin, because years ago it was not deemed prudent to trade by means of borrowed capital.

The connection between the foreign trade of this country and banking has been considered by various committees of the House of Commons at different intervals, from 1800 to 1847.

The development of the foreign trade of this country is one of the most important events in its commercial history. We see the results of such trade in the foreign exchanges, which illustrate the fluctuations in the price

to be paid for remittances to and from this country. The difference between the imports and exports must be paid by means of drafts, or bills of exchange, drawn upon the importer or exporter of goods, and the final balance is adjusted by means of specie, which is the only commodity that can finally settle international indebtedness.

CHAPTER III.

THE CURRENCY.

IT is desirable to consider the question of the currency separately, because, although banking is in many ways distinct from that subject, yet a series of events was the means of creating a close connection between the two. For example, the Bank of England had the privilege of issuing notes, and was also compelled to purchase gold at a certain fixed price.

Again, banking profits at the beginning of the last century were, to a great extent, dependent upon the amount of notes a bank could issue.

The subject of the currency was also the most prominent feature in the history of banking until some time after the passing of the famous Act of 1844.

In the early history of banking many erroneous ideas were held in consequence of the question of the currency being interwoven with the former subject. It was thought at one time that the currency laws were really the cause of the commercial disasters which have occurred in this country at stated intervals. Now, it is quite clear that loss of capital cannot be in any way connected with the question of bank notes, but unfortunately these two questions have been mixed together in a very confused manner. No doubt many of the early bankers lent their notes to

unsound borrowers, and by this means great disasters took place; but loss of capital was quite another matter.

At various times there has been too much capital converted from floating to fixed; and we have already referred to the former kind as that which a banker lends to his customer. If, on the other hand, capital is utilised for the purpose of constructing a railway, we should call it fixed, because a great number of years would elapse before it would be reproduced; when this takes place no alteration in the currency laws can alter the condition of capital. Many early writers said: Give us more notes, and then all these panics, etc., will disappear; but the nation, during periods of financial distress, does not require more notes, but capital. It is therefore important to recognise that gold and bank notes are only mere machinery required for a certain purpose. If notes and gold were abolished, other means, or *tools*, as Professor Price designates bank notes, would be found to carry on the interchange of commodities.

Prior to the passing of the Bank Act of 1844, bank notes had been at various periods below their par value. This was seen from the price of gold. In September, 1799, gold was £3 17s. 6d. per oz., but in June, 1800, the price of gold rose to £4 5s. per oz. Now this was due to the inconvertible bank notes in circulation.

The following table shows the depreciation:—

	Real Value of Bank Note.
1st September, 1797, to 19th October, 1798	£1 0 0
13th April, 1804, to 15th October, 1805	0 19 6
9th October, 1810	0 18 4
12th February, 1811	0 16 11
26th March, 1811	0 16 3
25th October, 1811	0 15 11
2nd October, 1812	0 14 5
22nd January, 1813	0 15 0
6th August, 1813	0 14 2

Whenever there is a fall in the value of bank notes in comparison with gold, it shows that there is an excess of paper money in circulation.

The country bankers supported all kinds of wild speculation by lending inconvertible notes, and when called upon to pay them were unable to do so. In the panic of 1793, out of 400 country banks no less than 100 stopped payment, and the remaining 300 were much shaken.

During the years 1814-1817 eighty-nine country banks suspended payment, and in the year 1825 no less than seventy-three collapsed in the same manner. The country bankers could at that period discharge their liabilities by means of Bank of England notes, and although such notes were at a discount, they were, nevertheless, a legal tender.

Such banking disasters called for a remedy; committees, both of the House of Lords and Commons, were appointed to inquire into the state of the currency. Most of the evils that had arisen were due to the suspension of cash payments by the Bank of England in the year 1797. The Bullion Committee of 1810 examined many witnesses in order to find out the cause of these disasters; some members stated that the bank notes were depreciated, and that the difference between the market price and the mint price of gold was the measure of the depreciation.

On the other hand it was asserted that notes were not depreciated, but that the price of gold had risen. The Committee, however, came to the conclusion that the suspension of cash payments by the Bank of England *had caused the depreciation of the paper*, and as soon as the Bank paid its notes in gold it would be advantageous for the country.

It seems hardly credible that such a simple question should have been disputed; whenever a note cannot be

converted into gold on demand, it must depreciate in value. If the holder of an inconvertible note wishes to purchase goods, and tenders it for payment, the seller might accept the same, but only at a discount. Thus goods are inflated in value when notes remain inconvertible; one of the disadvantages of an inconvertible paper currency is great fluctuations in prices. Bank notes in the present day are worth their face value, because it is known that on demand gold can always be obtained in exchange.

The Restriction Act, passed in 1797, prevented the Bank from cashing its notes in gold. The Government stated that the gold held in reserve would leave the country, unless steps were taken to prevent it. Thus, in the years preceding 1819 the Bank was frequently ready and anxious to pay in specie.

The evil results of this restriction, which caused depreciated bank notes, were at last seen, and an Act of Parliament was passed making it compulsory on the part of the Bank of England and the country bankers to pay their notes on demand.

The Bank Restriction Act was continued absolutely from 5th July, 1819, to 1st February, 1820, when the Bank was permitted to pay notes in gold as follows, *viz.*:—

(1) Between 1st February and 1st October, 1820, the Bank was required to pay its notes in gold bullion of standard fineness at the rate of £4 1s. per oz., but only notes of the value or price of 60 oz. of gold could be exchanged.

(2) Between 1st October, 1820, and 1st May, 1821, the Bank was required to pay its notes in gold bullion at the rate of £3 19s. 6d. per oz.

(3) Between 1st May, 1821, and 1st May, 1823, the

Bank was to pay in gold bullion upon the same plan at the rate of £3 17s. 10½d. per oz., being the Mint price of gold.

(4) From 1st May, 1823, the Bank was to pay its notes in the gold coin of the realm.

(5) Finally, all the laws which restrained the exportation of gold were abolished, and it was allowed to be exported or melted without incurring any liability.

The Bank of England commenced paying off its notes under £5 in 1821, and the country bankers were allowed to issue notes under £5 until 1833.

The Restriction Act mentions the price of gold as £3 17s. 10½d. per oz.; now, as this concerns the metallic currency of the country, perhaps it will be more convenient first to consider the relation of banking to this subject before stating the still greater changes in the paper currency.

In the year 1816 it was enacted that gold alone should be the legal standard of value, but silver would only be tender of value to the extent of 40s. From the reign of William I. to that of Henry III. we had in this country a silver currency; gold coins were then gradually introduced as the wealth of the country increased. The value of the guinea was fixed at 21s. in the year 1717, but the sovereign took its place on 1st July, 1817.

The weight of the English sovereign is 123·27447 grains of English standard gold, there being 1 part of alloy to 11 parts of fine gold. And from the weight of the sovereign we get the Mint price of gold, *viz.*, £3 17s. 10½d. per oz.

The Mint cannot issue a coin of less weight than 123·074 grains, or of a greater weight than 123·474 grains.

The quantity of gold which the nation ought to have in reserve to meet sudden demands is a question of considerable difficulty.

Bronze coin is only a legal tender for 1s. ; country bank notes, although still forming part of the currency, do not constitute a legal tender for payment of a debt.

The late Mr. Bagehot advocated the keeping of a large reserve of gold by the Bank of England ; he showed that the Bank is now the only place where it can be obtained in large quantities to meet any sudden demand. All the surplus coming into the country finds its way into the vaults of that institution, because the other bankers do not keep any appreciable reserve of the metal. The London bankers can always obtain gold from the Bank of England, since they have accounts with that institution ; but recently it has been suggested that it would be desirable for some of the large banks to hold a secondary cash reserve.

The Bank of England is thus called upon to meet the requirements of the United Kingdom, and also to settle the differences of international trade. Formerly the effects of a bad harvest were to cause a sudden drain of gold to pay for foreign corn to make up the deficiency. All the spare money of the country bankers and of the Irish and Scotch banks is sent to the Metropolis, and lodged with their London agents, who keep their cash reserves at the Bank of England ; consequently, the latter institution becomes the final cash reserve of the country.

It has been stated that the bankers' balances at the Bank of England ought not to be utilised in the same manner as ordinary deposits by that institution, because of this unique system.

The increase in the metallic reserve of the Bank of England from the year 1850 is seen from the following table :—

£
1850 = 15,500,000
1855 = 11,000,000
1860 = 13,000,000
1865 = 14,000,000
1870 = 23,000,000
1872 = 24,000,000
1874 = 21,500,000
1875 = 22,000,000
1880 = 27,663,000
1885 = 24,173,000
1890 = 21,818,000
1903 = 34,000,000

Mr. Jevons stated in 1875 that the metallic circulation of the country was as follows, *viz.* :—

Gold coin in circulation	= 100 millions.
Bullion in the Bank of England	= 15 „
Silver	= 15 „
Bronze	= 1½ „
	<hr/>
	£131½ millions.

Although Mr. Bagehot insisted upon a large cash reserve, yet we must remember that the country only requires enough gold to interchange commodities, etc. If ever there exists a want for the circulating medium, it can, as a rule, be obtained by raising the rate of interest, and thereby attracting gold from abroad.

Another remedy for a deficient supply may be found in a greater use of cheques for small amounts, temporarily, until we obtained our usual reserve.

Lord Avebury states that gold is now very little used in comparison with cheques; a sum of £19,000,000, paid into Messrs. Robarts, Lubbock & Co.'s bank, was made up as follows :—

Cheques and bills	£18,395,000
Notes	487,000
Coin	118,000
	<hr/>
	£19,000,000

Thus the cash was only 3 per cent., and the coin only $\frac{1}{2}$ per cent., of the total transactions.

If we compare the metallic circulation of the country with the note circulation, we find that the former has increased rapidly in comparison with the latter.

1819 note circulation, England and Wales .	£40,000,000
1870 " "	30,000,000
	<hr/>
Less	£10,000,000
1819 metallic circulation	£10,000,000
1870 " "	105,000,000
	<hr/>
More	£95,000,000

In the year 1844 the gold circulation was £36,000,000, and the note circulation £37,000,000, the notes therefore being slightly in excess.

The use of cheques has increased to an enormous extent in recent years: for example, in the year 1844 the Clearing House returns were equal to 40 times the note circulation; but for 1903 the returns of the former were 177 times more. This tends to show that a less amount of gold is now required in consequence of its being superseded by cheques, combined with other economical methods, such as the use of telegraphic transfers. Again, the greater rapidity in the circulation of money diminishes the amount of coin required. We must always consider gold as a *tool* required to do certain work in the interchanging of goods. At present it is the best metal because of its great value: but, if large quantities were found, it would, like silver, depreciate in value. This depreciation might so increase that it would be the means of raising the value of other commodities measured by gold. It must not be forgotten that the price fixed is, after all, an arbitrary one, and, as it does not vary, we must get fluctuations in the value of commodities.

The country is not benefited by the import of large quantities of gold, unless required for the purpose of circulation. If there is a very large amount at the Bank of England, it shows that there is very little demand for capital.

Of course, it is very important that the Bank of England notes should always be convertible into gold, and for this reason a fair reserve is necessary; but it must be remembered that the Bank has never been called upon to discharge its liabilities on *notes*, even at the most critical periods in the history of banking.

With these few remarks upon the gold currency we will now return to our former subject, *viz.*, the note circulation.

On the 19th June, 1828, an Act was passed which enabled bankers in England to issue certain unstamped promissory notes and bills of exchange upon payment of a composition in lieu of the Stamp duties thereon. The object of this Act was chiefly to give country bankers the same advantages in respect of drafts as were granted to the branches of the Bank of England. In the following month of the same year notes under £5 were forbidden under certain penalties. During the session of 1832 a Committee of the House of Commons discussed the question of the paper currency under the following sections:—

(1) Whether the paper circulation of the Metropolis should be confined to the issue of one bank, or whether there should be a competition of different banks of issue, with an unlimited number of partners.

(2) Whether the note circulation of the country should be confined to one bank.

(3) What check should be provided to secure for the public a proper management of the banks of issue, and especially whether it would be expedient and safe to compel them periodically to publish their accounts.

The Committee did not draw up any report on these points, but from that time the Bank of England published a weekly statement of its accounts.

The crisis of 1836 brought the question of the currency again before the country. Lord Overstone stated that it was desirable to separate banking functions from the management of the currency.

In the year 1840 a Committee was again appointed to consider the effect of the paper currency on the country. Perhaps it will be as well to state the different opinions expressed upon this question prior to the passing of the famous Act of 1844.

Lord Overstone and Sir Robert Peel represented one party, and Mr. Tooke and Mr. Fullarton the other.

Lord Overstone and Sir Robert Peel held:—

(1) That the amount of circulating medium may be greater or less than is properly required for the transaction of the current business of the community, and that where greater it tends by the excess to make the use of the circulating medium too cheap.

(2) As prices are measured by the circulating medium it enhances their price.

(3) That such enhancement, by reducing exports and stimulating imports, turns the foreign exchanges against us, and leads to a drain of bullion.

(4) If the circulating medium be too low the opposite effect is produced in favourable exchanges and an influx of bullion.

(5) The principal cause of an undue expansion of the circulating medium is due to a too large amount of bank notes payable on demand.

(6) Issuers of notes can regulate at will the amount of them in circulation.

(7) If notes are kept in proper proportion to the bullion

the amount of the circulating medium will be prevented from becoming greater than it should be, and the mischief held to arise will be avoided.

Mr. Tooke and Mr. Fullarton held:—

(1) That no greater amount of gold or notes is in circulation than is required by the current transactions of the country. If there is more it is hoarded up by the bankers.

(2) That while a large portion of the circulating medium is dependent solely upon the credit of its issuers, its extensions can in part only be limited by the state of that credit on one hand, and by the aggregate demand of those who are willing to pay for its use on the other.

(3) That while there is a large fund of deposits in the banks issuing, a banker cannot affect the aggregate amount of circulating medium by issuing or withdrawing notes.

(4) A restriction of notes must be ineffectual, because bank notes only represent one portion of the addition made by the operation of bankers.

(5) That the true measure of the voluntary addition made by a banker is to be found in the terms upon which he makes his advances.

(6) That any attempt to control the issuing banker by law would be, in fact, an attempt to fix the price of the use of money.

These different opinions show that the subject of the currency was not clearly understood.

After the passing of the Act of 1844, great disappointment was felt, because the great changes which it was supposed to accomplish did not take place.

No doubt the Act was good in some particulars; for example, the convertibility of the note was secured, but commercial crises, panics, drains of gold, large issues of notes and high rates of interest were as frequent after

the year 1844 as they were previous to the passing of the Act.

The gradual extinction of the country bank issues was no doubt one of the principal objects intended, and it will be seen that the provincial circulation of notes has gradually diminished; but whether this was advisable or not is a question which has been much disputed.

The failure of many banks of issue was the chief reason why the Government by this Act intended to exercise some control over the note circulation. One of the popular errors with regard to paper money was that a banker could issue to an unlimited extent. Now, the number of notes issued depends entirely upon the wants of the people; the banker cannot make his customers accept notes, although he might be desirous of circulating a large amount.

Again, the Bank of England cannot control its issue of notes, because any number can be obtained from that institution in exchange for gold. It was also supposed that notes could be issued, and that a certain amount of gold would always be held. Now this is impossible, because so long as notes are in circulation, gold can be obtained for them on demand. It is therefore possible to drain the Bank of England of all the gold in its possession. We must remember that there is no creation of capital by a banker issuing notes, which only represent capital lent; the holder of a note is really the lender of capital, although it appears that the banker is acting in that capacity. In this manner the banker makes a profit on the capital entrusted to him through the medium of his notes.

It has been disputed whether the issue of £15,000,000 of notes by the Bank of England *against securities* is sufficient; but when that institution was allowed to issue

to any amount, without holding gold against the excess, in the years 1847, 1857 and 1866, it was only in 1857 that an excess occurred, and then only for the comparatively small sum of £800,000.

Notes economise capital, because without them a larger amount of gold would be required for circulation. It is very important that they should be always convertible, and in order to secure this the Bank of England raises the rate of interest when the amount of gold held in reserve appears too small.

The Government, in consideration of the privileges given to that institution in respect of the note circulation, receives in return about £175,000 per annum, which is really a part of the Stamp Duty.

With these remarks upon bank notes we will now consider the leading provisions of the famous Bank Act of 1844, by which the currency of our country is now definitely settled.

CHAPTER IV.

BANK ACT OF 1844.

FROM and after 31st August the Issue Department of the Bank of England shall be separated from the Banking Department; that the Issuing Department may issue notes to the extent of £14,000,000 upon securities set apart for that purpose, of which the debt of £11,015,100, due from the Government to the Bank, shall form a part; that no amount of notes above £14,000,000 shall be issued except against gold coin or gold or silver bullion, and that the silver bullion shall not exceed one quarter of the amount of gold coin or bullion.

Any person is entitled to demand notes from the Issuing Department in exchange for gold bullion, at the rate of £3 17s. 9d. per oz.

Should any banker discontinue his issue of notes, the Bank of England may, upon application, be empowered by an Order of Council to increase its issue to the extent of two-thirds of the issue thus withdrawn, but all the profit of this increased issue must go to the Government.

The Bank of England is allowed to compound with issuing banks, consequently forty-three banks in England made agreements to that effect with the Bank of England. The Bank of England is exempt from Stamp Duty.

No new banks of issue shall be formed.

That bankers claiming to issue notes shall send a return of their circulation during the twelve weeks next preceding the 27th April, 1844, in order to obtain the average amount of the same.

Banks uniting need not give up their note issue, provided that it shall not be lawful for any such united bank to issue notes at any time after the number of partners therein shall exceed six persons.

Every banker must transmit a weekly account to the Commissioner of Stamps and Taxes.

Certain penalties are incurred by issuing more notes and not making returns in accordance with the Act.

The Bank of England's weekly account should be in the following form :—

ISSUING DEPARTMENT.

Notes issued.	Government debt.
	Other securities.
	Gold coin and bullion.
	Silver bullion.

BANKING DEPARTMENT.

Proprietors' capital.	Government securities.
Rest.	Other securities.
Public deposits.	Notes.
Other deposits.	Gold and silver coin.
Seven-day and other bills.	

In 1854 bank notes were defined by Act of Parliament as “ bills, drafts or notes issued by a banker for the payment of money to bearer on demand, and which shall entitle the holder thereof, without endorsement, to the payment of any sum of money on demand, whether the same shall be expressed or not, in whatsoever form shall be deemed to be bank notes ”.

There has been a great increase in the note circulation of the Bank of England :—

AVERAGE AMOUNT HELD BY PUBLIC

	£
1718 =	1,829,930
1778 =	7,030,680
1790 =	10,217,000
1800 =	15,450,000
1810 =	23,904,000
1819 =	25,657,610
1830 =	20,620,000
1840 =	17,231,000
1844 =	20,250,000
1850 =	19,520,000
1861 =	20,010,000
1865 =	21,090,000
1870 =	23,300,000
1875 =	27,346,000
1880 =	26,915,000
1885 =	24,667,000
1890 =	24,961,000
1895 =	25,870,000
1901 =	29,558,000

From these tables we observe that from 1844 to 1901 the increase has been about £10,000,000. This is more clearly seen if we compare the note circulation of the United Kingdom with the increase in the number of bank offices and also with the population.

Thus, while the population between 1851 and 1878 grew 23 per cent., the circulation of bank notes was 35 per cent., and although the bank offices had increased 91 per cent., which would mean a greater use of cheques, there was still a great development in the note circulation.

The following table will show the present position of the issue of English country banks in 1903 :—

	Private Banks.		Joint-Stock.		Together.	
	No.	Auth. Issue.	No.	Auth. Issue.	No.	Auth. Issue.
By Act of 1844	207	£5,153,407	72	£3,495,446	279	£8,648,853
Since ceased to issue .	182	£4,385,619	52	£2,340,079	234	£6,725,698
Amalgamated without loss of issue	6				6	
	188				240	
Remaining	19	£767,788	20	£1,155,367	39	£1,923,155

The following table shows the decrease in the average circulation of country banks since 1844 :—

£
1844 = 8,170,000
1850 = 6,320,000
1855 = 6,850,000
1861 = 6,110,000
1865 = 5,800,000
1870 = 4,890,000
1875 = 4,812,000
1880 = 3,400,000
1885 = 3,036,000
1890 = 2,367,073
1895 = 1,747,925
1903 = 677,000

There has been a diminution of 43 per cent. in the issue of private banks, and 55 per cent. in joint-stock banks. Of the issue of joint-stock banks, 74 per cent. was compulsorily forfeited under the Act, and 26 per cent. by bankruptcy. Of the issue of private banks, 32 per cent. was forfeited under the Act, 21 per cent. was given up voluntarily, and 47 per cent. was lost through bankruptcy.

Authorised issue lapsed :—

	£
1844-48 =	423,410
1849-53 =	282,981
1854-58 =	234,174
1859-63 =	173,212
1864-68 =	753,814
1869-73 =	157,099
1874-75 =	163,178
	<hr/>
	£2,187,868
1875-95 =	2,236,363
1895-1903 =	2,301,467
	<hr/>
	£6,725,698

In consequence of the above lapsed issues the Bank of England authorised circulation has increased from £14,000,000 to £18,450,000.

The large amount cancelled in 1864-68 was principally due to the National Provincial Bank giving up its issue on opening a London office, but since that date there has been a further decrease of £3,450,000, due to the amalgamation of private and joint-stock banks with London institutions.

It will be seen that there has been a great diminution in the issues of country banks, caused either by bankruptcy or amalgamation. The latter cause is an important one; the recent amalgamation of the Smiths' Banks with the Union Bank of London involved the cancellation of £221,460. There is no doubt that in a few years the whole issue will practically disappear; the great development of railway facilities, combined with the opening of branches in small towns, which increases the circulation of country cheques, will contribute largely to this extinction.

The banks issuing notes within sixty-five miles of London have diminished in much greater proportion than those beyond, which is due to the fact of their nearness to London.

It may be noticed that the country note circulation is usually less in August than in May, the difference being about £500,000.

The late Mr. Jevons prepared a statement showing the variations from week to week from 1845 to 1862 :—

In 18th week of the year	.	.	.	£6,920,000
„ 31st „ „	.	.	.	6,370,000
Diminution .				<hr/> £550,000
In 19th week of the year	.	.	.	£6,900,000
„ 32nd „ „	.	.	.	6,350,000
Diminution .				<hr/> £550,000

Bank of England notes are a legal tender for payment of debts in England, but not in Scotland. With regard to country bank notes, they are a legal tender if not objected to on that account, but the holder must circulate or present them for payment the next day after their receipt if he wishes to charge the transferor in case the banker fails. The holder, in fact, must treat country bank notes as cheques, in order to preserve his rights to sue in case of dishonour.

The Banking Act passed in 1879 allowed the English joint-stock banks to protect their note issue by stating in the articles of association that the term limited liability does not apply to the note issue, and that shareholders will continue liable in respect of notes issued in the same manner as an unlimited company.

CHAPTER V.

NOTE CIRCULATION OF SCOTLAND.

THE note circulation of Scotland is in many ways distinctive; for example, the issue of £1 notes shows that the circulation was adapted to the wants of the people. Thus, in 1879, out of a total circulation of £5,522,000, no less than £1,974,000 represented £1 notes.

Another point to be noticed is the great confidence which the Scotch people have in their note circulation.

The issue of notes in Scotland is now regulated by the Act of 1845, but previous to that year any bank could be formed with the privilege of issuing notes.

The opposition to the Act of 1845 was overcome by giving the existing banks the sole right of issue, which practically meant the exclusion of new banks in that country.

This Act imposed unequal conditions; for example, one bank was allowed to issue £1 for every £11 18s. 7d. of capital, whilst another could issue the same amount for £2 5s. 8d. of capital. The Act also compels the banks to keep gold in their vaults for the excess above the authorised issue.

There is always a large increase in the note circulation in May and November, consequent on the payment of rents, etc., being made on 15th May and 11th November. At these periods of the year large sums of gold are

obtained from the Bank of England and sent down to Scotland in order to enable the Scotch banks to make their returns in accordance with the Act of 1845.

This hypothecated gold very soon finds its way back to the Bank of England after the returns are made up. It is estimated that the Scotch banks make a profit of about 2s. 6d. per cent. on their note circulation.

We will now state the leading provisions of the Act of 1845 :—

(1) Scotch banks are allowed to retain their £1 notes.

(2) The power of issuing notes is confined to those banks that issued notes in the year preceding 1st May, 1845.

Banks amalgamating are allowed to retain the aggregate fixed issue of the separate banks. They may exceed the circulation limit, but the excess must be represented by coin. A return must be made to the Stamp Office of the average amount in circulation of the preceding four weeks. If notes are in excess of the authorised circulation, and gold is not kept in reserve against such excess, then the bank which infringes the law must forfeit the amount not covered by specie.

The returns are made as follows :—

TEN SCOTCH BANKS—AUTHORISED ISSUE, £2,676,350.

Average circulation during four weeks ending 29th August, 1903 :—

£5 and upwards	£2,286,381
Under £5	5,314,019
Total	£7,600,400
Average amount of gold and silver coin held . . .	£6,376,910

Bank of England notes are not a legal tender in Scotland.

The Government reserves to itself the right of inspecting the books of the banks in order to ascertain the correctness of the returns.

The following tables show the present position of the note issue in Scotland :—

	Banks.	Fixed Issue.
By Act of 1845	19	£3,087,209
Reduction by Amalgamation	6	
Failure of Western Banks, including Ayrshire Bank	2	337,938
	<hr/> 8	
Balance	11	£2,749,271
City of Glasgow	1	72,921
	<hr/> 10	<hr/> £2,676,350

THE AVERAGE CIRCULATION SINCE 1844.

£	Over Limit of Act, 1845. £
1845 = 3,020,000	210,000
1850 = 3,220,000	140,000
1855 = 4,100,000	1,020,000
1861 = 4,200,000	1,450,000
1865 = 4,380,000	1,630,000
1870 = 5,110,000	2,360,000
1872 = 5,320,000	2,570,000
1874 = 5,904,000	3,227,650
1876 = 6,099,000	2,227,650
1880 = 5,550,000	2,873,650
1885 = 5,745,000	3,068,650
1890 = 6,276,323	3,599,973
1895 = 6,938,879	4,262,529
1903 = 7,891,000	5,214,650

The note circulation of Scotland has increased in far greater proportion than the population, which shows that bank notes are in great favour in that country.

The English bankers complain that the Scotch banks have privileges which they do not possess, and state it would be impossible for any bank to succeed in Scotland unless allowed to issue notes, which is prevented by the Act of 1845.

It seems an anomaly that Scotch banks should be

allowed to retain the right of issuing notes when they opened London offices, whilst the English country banks are obliged to surrender their note circulation on so doing. Of course, when the Act was passed, it was not contemplated that the Scotch banks would compete with the existing banks in the great Metropolis.

CHAPTER VI.

NOTE CIRCULATION OF IRELAND.

THE note circulation of Ireland was finally settled by the Act of 1845. The authorised issue, like that of the Banks of Scotland, was to be the average amount of the year ending 1st May, 1845. If any two banks amalgamate, the new institution may issue to the amount of the circulation of the united banks. If any bank voluntarily surrenders its right, and agrees to issue Bank of Ireland notes, the latter institution may increase its authorised amount to the extent of the sum lapsed. This provision is quite different from the Act relating to Scotland.

In Ireland all notes must be payable at the place or places where they have been issued or reissued, whilst in Scotland notes issued at the branch office are payable only at the head office. The amount of gold held for the excess of the authorised circulation in Ireland must be held at the chief office, or at four chief places of issue.

No new bank of issue can be formed. The circulation of notes in Ireland was in private hands until the establishment of the Bank of Ireland in 1782 with a monopoly of banking; but an Act, passed in 1821, allowed joint-stock banks to issue notes, provided they had no office in Dublin, or sixty-five miles beyond.

When the Act of 1845 was passed no private bank issued notes in this country.

The following table shows the increase in the note circulation of Ireland since 1844 :—

AVERAGE CIRCULATION.

	Limit of Act, 1845. Above or Under.
£	£
1844 = 5,940,000	— 414,000
1850 = 4,510,000	— 1,840,000
1855 = 6,360,000	+ 6,000
1861 = 6,260,000	— 90,000
1865 = 5,980,000	— 370,000
1870 = 6,880,000	+ 526,000
1875 = 7,064,000	+ 710,000
1880 = 6,548,000	+ 194,000
1885 = 6,225,000	— 129,494
1890 = 6,838,716	+ 484,222
1895 = 6,400,123	+ 45,629
1903 = 7,000,636	+ 646,142

The eight banks which issued notes were reduced to six by amalgamation, but the fixed issue remained the same, viz., £6,354,494.

The returns are made as follows :—

SIX IRISH BANKS—AUTHORISED ISSUE, £6,354,494.

Average circulation during four weeks ending 29th August, 1903 :—

£5 and upwards	£4,229,221
Under £5	2,544,873
Total	£6,774,094
Average amount of gold and silver coin held . . .	£3,623,121

The effect of the bad harvests in Ireland, and also the social and political disturbances in that country, is exemplified by the note circulation in recent years. Thus, comparing 1879 with 1878 there is a fall of 13 per cent. If we compare the laws which regulate the English country note circulation with those regulating the Irish and Scotch issue, we observe that £1 notes are only allowed to be issued in Scotland and Ireland. Again, Bank of England notes are not a legal tender for money either in Scotland or Ireland.

The English banks cannot exceed the limit fixed by the Act of 1845, whilst the Irish and Scotch banks can do so if they keep the excess of such issue in gold. The English banks make a return of their weekly circulation, whilst the Scotch and Irish banks return a monthly account of their issue.

CHAPTER VII.

BANK OF ENGLAND.

THE Bank of England owes its origin to William Paterson, a Scotchman, who, in 1693, proposed that the expenses of the war with France should be met by a national loan. Forty merchants subscribed £500,000 towards the sum of £1,200,000, which was lent to the Government at the rate of 8 per cent. per annum. For this consideration, the subscribers were to be made a corporation, under the title of the Governor and Company of the Bank of England.

The Act passed in 1693 stated : “ Their Majesties may make commissioners take subscriptions for £1,200,000 ” ; and section 20 states : “ Their Majesties may appoint rules for transferring, and make the subscribers a corporation by the name of the Governor and Company of the Bank of England ”.

The Bank of England did not originally have the sole monopoly of joint-stock banking, but when it was proposed to start another bank in 1708, on the same principles, the directors succeeded in obtaining that monopoly.

The Charter was renewed in 1697, 1708, 1713, 1716, 1721, 1742, 1746, 1749, 1764, 1781, 1800, 1808, 1816, 1833 and 1844.

The late Mr. Bagehot some years ago stated that the

monopoly given to the Bank of England was injurious for the following reasons, *viz.* :—

(1) Banking ought to be free, because monopolies are likely to be injurious to the public unless kept within reasonable limits.

(2) The Bank, being in some indirect manner connected with the Government, is supposed by many to be in reality a Government institution.

(3) By this means it had a better reputation than other institutions of a like character.

(4) When crises, panics, etc., occur in the country, it was expected to lend money to all comers.

(5) Finally, in consequence of this monopoly, it became the sole cash reserve for the country.

This statement is no doubt true to a certain extent, but the rapid growth of the English joint-stock banks in recent years has somewhat altered the position.

It is in many ways desirable that we should have a central institution, governed on somewhat different principles to our leading banks. A bank which holds to a great extent the cash reserve of the country, and also has the privilege of issuing legal tender notes, will always be an institution of great importance.

Although the deposits held by the Bank of England are somewhat small in comparison to some of the large joint-stock banks, yet it still remains a great power in the money market.

The gold reserve of this country is largely under its control, and it is able therefore to replenish that reserve when the necessity arises.

The Bank of England is managed by a governor, a deputy-governor, and twenty-four directors. The late Mr. Bagehot thought it would be better if the Bank had a

permanent head rather than a continual change of governors. The re-election of Right Hon. W. Lidderdale during the Baring crisis showed somewhat the necessity of having a permanent governor. The Bank of France has a permanent head, the governor being elected by the Government, and holds his appointment for life.

The influence and position of the Bank of England during the eighteenth century was far greater than in the present day. The London bankers were then very jealous of its position because of its large capital; the large issue of notes made it a very formidable opponent.

Another interesting fact is that it became the chief factor in the money market, and, holding that position, fixed the price for the loan of capital. We can understand how this occurred when we recollect that it was the only joint-stock bank in existence, and as such held large deposits in comparison to the private banks.

We have stated that the rate of interest fixed by the Bank of England became the market rate, and at the present time it remains so, although perhaps to a less degree.

The London joint-stock banks have to some extent abandoned the method of allowing interest on deposits to be governed by the Bank rate.

The Bank of England is comparatively a small lender of money, so that its rate does not indicate the real value of money in the market. We must ascertain exactly the *whole* supply of capital and demand for it before we can ascertain the correct rate of interest. Including loans and discounts the Bank lends less than $\frac{1}{3}$ of the amount lent by the London joint-stock banks, and less than $\frac{1}{5}$ of that lent by the London bill brokers.

However, as a lender of capital, it has always exercised great caution, and only made advances upon the

best securities. The capital of the Bank amounts to £14,553,000, which is enormous compared with the capital of other banks, and tends to keep the dividends low. Thus, from 1797 to 1822 the dividends were from 10 per cent., and from 1817 to 1876 the average was 8·6 per cent. The dividends in recent years have been 10 per cent.

The Bank was started on condition that a certain sum, *viz.*, £1,200,000, should be lent to the Government. The increase in the following years was due to further loans to the Government of the day, and in return it obtained renewals of its charter, and also other advantages.

The following table shows when loans were made to the Government, and the balance of debt still due to the Bank of England :—

	£
1694 =	1,200,000
1708 =	2,175,000
1716 =	4,175,000
1721 =	9,100,000
1742 =	10,700,000
1746 =	11,681,000
1816 =	14,686,000
1844-76 =	11,015,000
BANK OF ENGLAND—DEBT.	
1694	£1,200,000
1708	400,000
1742	1,600,000
	<hr/>
	£3,200,000
1721 Balance of Capital Stock purchased of South Sea Co.	£3,328,300
1716 Balance of Exchequer Bills	500,000
1727 Advance to Government	1,750,000
1728 " "	1,250,000
1746 Exchequer Bills given up to be cancelled	986,800
	<hr/>
	£11,015,100

The following table shows the increase in its liabilities :—

£

1797 =	13,770,390
1833 =	30,937,000 (including notes)
1844 =	14,500,000
1850 =	18,800,000
1855 =	17,800,000
1865 =	21,200,000
1872 =	29,300,000
1885 =	32,630,000
1895 =	46,000,000
1903 =	49,000,000

Since the passing of the Bank Act of 1844 its reserve for the period from 1846 to 1891 has diminished in proportion to liabilities—

from 1846-54 = 51 per cent.

„ 1864-72 = 42 „

„ 1885-91 = 42 „

but in 1895 the proportion increased to 58 per cent. The average for four months in 1903 was 48 per cent.

In this country the Bank of England is the only institution where large amounts of gold can be obtained in order to meet home and foreign demands. Its position, therefore, as a bank of discount is very often impeded, since the rate of interest is advanced in order to prevent the reserve of gold getting too low.

It has been mentioned that the Bank Act of 1844 divided the issue from the banking department, and from that time the two offices were kept separate.

The weekly returns were to be drawn up as follows :—

AUGUST 19, 1903.

ISSUE DEPARTMENT.

Notes issued . . .	£51,830,000	Government debt .	£11,015,000
		Other securities . .	7,160,000
		Gold coin and bullion	33,655,000
			<hr/>
			£51,830,000

BANKING DEPARTMENT.

Proprietors' capital.	£14,553,000	Government securities	£20,544,000
Rest	3,528,000	Other securities . . .	25,063,000
Public deposits . . .	8,660,000	Notes	22,488,000
Other deposits . . .	43,311,000	Gold and silver coin .	2,082,000
Seven-day and other bills	125,000		
	£70,177,000		£70,177,000

The business of the Bank of England consists of three groups or divisions, *viz.*: (1) The management of the National Debt. (2) Issue of bank notes. (3) Government and private banking.

The Government pays the Bank about £180,000 per annum for undertaking the entire management of the National Debt, which at present amounts to £798,349,190.

Although no interest is allowed on deposits, in recent years they have increased to a large extent, showing the confidence which the public have in that institution.

ANNUAL AVERAGE OF DEPOSITS.

£

1844 =	13,300,000
1850 =	17,600,000
1855 =	16,800,000
1860 =	20,100,000
1865 =	20,700,000
1872 =	28,800,000
1875 =	26,413,000
1880 =	32,950,000
1885 =	33,451,000
1890 =	33,364,000
1895 =	40,556,000
1902 =	51,955,000

Whenever there has been in this country a want of confidence in our banking institutions, which has resulted in a withdrawal of deposits, the Bank of England has been an exception, because at such periods its deposits have increased. In many respects we may consider it a model institution, and the conservative policy of the directors has been beneficial to the country. As a bank of issue, and

holding the gold reserve, its management has at various times been criticised, but it cannot be said that money has been lent to support reckless speculations; it is desirable that we should have a bank governed on independent lines. Competition is in many ways beneficial, but in the case of banking it is somewhat dangerous.

We have already referred to the issue of bank notes, and it is therefore only necessary to refer to the third division, *viz.*, Government and private banking.

With regard to the Government or public deposits, they fluctuate considerably, and are dependent upon the requirements of the Government. For example, when the Income Tax becomes due, we should expect to see a large increase in the amount.

The public deposits vary considerably according to the requirements of the Government; it has been stated that in the interest of the money market it would be desirable if the Government account was divided amongst the various banks of the Metropolis, on the understanding that such banks should hold Government securities against the balances. This would have prevented large withdrawals of available capital from one institution instead of from a large number. Under these circumstances each bank would be required to keep a certain reserve against the said balances.

The seven-day and other bills issued have diminished considerably; in the year 1844 they were more than £1,000,000. now they only amount to about £120,000. The great decrease in these bills is no doubt due to the greater facilities offered by the joint-stock banks of the country which issue drafts payable in London.

The "other deposits" stated in the weekly report include the bankers' balances, which certainly ought to be utilised by the Bank with great caution, because they

represent the cash reserve of the banks of this country. As a rule, sufficient cash is only kept in the tills of each bank for daily requirements. Thus, as Mr. Hankey stated, "when the bankers' balances are very large, the Bank does not utilise the increased amount". These balances form a part of the cash reserve of the various banking institutions, and the amount has increased considerably in late years. If the London banks held their own cash they would no doubt, collectively, have a larger reserve; we may therefore occasionally notice fluctuations in the rate of discount due to the Bank holding such deposits.

We will now consider the Assets in the Banking Department.

The Government securities are about £15,000,000; so that more than the whole of the capital of the Bank is invested in interest-bearing securities.

The amount of the other securities has increased as follows :—

	£
1844 =	9,400,000
1850 =	11,100,000
1855 =	15,300,000
1865 =	20,500,000
1870 =	18,600,000
1872 =	21,400,000
1892 =	29,777,000
1902 =	29,684,000

Such other securities include the bills discounted, and from a Government return, made in 1872, one was able to ascertain the amount of advances. It is to be regretted that a similar return has not been made since, because one could then form some idea of the bill transactions of the country. From this return it will be seen that the fluctuations in recent years of the remainder, after deducting the temporary advances and bills discounted, were small.

	£
1844 =	5,400,000
1850 =	7,200,000
1855 =	8,700,000
1860 =	11,100,000
1865 =	9,500,000
1870 =	8,500,000
1872 =	10,600,000

With regard to temporary advances, they were three times more in 1844 than in 1872, as follows :—

1844	£3,900,000
1872	1,300,000

The bills discounted from 1844 to 1872 have fluctuated greatly, which is due to the fact that any one properly introduced may have a discount account. This is quite a different method from that of the other London banks. However, the Bank as a discounter of bills does not occupy in the present day the same position as in former years, which is due to the fact that, in consequence of the growth of capital, we have in the present day large joint-stock banks and discount companies.

The competition between the Bank and the outer market is sometimes great; if the rate of discount is below that of the outer market, there will be a large increase of business from outsiders. This would cause a demand, and consequently the rate of interest rises.

In consequence of competition in recent years, the Bank stated that, although the published rate was the official minimum, yet under certain conditions it would discount bills at a lower rate of interest.

During commercial crises the bills discounted have been a large amount, because every one expects the Bank at such times to lend money in the shape of loans and advances.

Mr. Hankey, in his work on *The Principles of Banking*, says “ that the Bank ought never to have encouraged this

opinion, but at these periods it has been found expedient to lend freely". In the year 1825 the directors stated : " The Bank had taken a firm and deliberate resolution to make common cause with the country ".

There is no doubt that the somewhat critical position of the Bank during the commercial crises of 1847, 1857 and 1866 was almost entirely due to monopoly. If banking had been free, the risks which attend banking operations would have been minimised, and the business divided amongst a greater number of banking institutions, so that the failure of one bank would not be so disastrous.

The causes of the fluctuations in the Government deposits will be more fully explained when we consider the question of the Bank rate of discount.

At the present time the joint-stock banks have larger reserves, and therefore are not so dependent upon the Bank of England during commercial crises.

The following table shows the average amount of bills discounted during the period when they were separated from the advances :—

	£
1834 =	1,800,000
1844 =	2,700,000
1855 =	6,000,000
1866 =	9,600,000
1868 =	5,000,000
1872 =	6,900,000
1873 =	7,737,000
1874 =	4,665,000
1875 =	4,402,000

The average rates of discount have decreased in recent years, although the war in South Africa caused a temporary increase in the value of money.

Average rate from 1844-56	=	£3 15s. 3d. per cent.	
„ „ 1857-72	=	£4 3s.	„
„ „ 1890-94	=	£3 1s. 10d.	„
„ „ 1898-1902	=	£3 12s.	„

The latter half of the year always shows the highest rates ; this is in consequence of more business being transacted in autumn and early spring.

AVERAGE RATES.

	£	s.	d.
1875 =	3	4	8
1876 =	2	12	1
1877 =	2	18	0
1878 =	3	15	8
1879 =	2	10	4
1885 =	2	17	7
1891 =	3	5	2
1892 =	2	10	7
1893 =	3	1	0
1894 =	2	2	3
1895 =	2	0	0
1900 =	3	19	3
1901 =	3	14	4
1902 =	3	6	6

The action of the Bank during commercial crises we shall subsequently consider. Since the year 1825 many facilities have been granted to the customers of the Bank, *viz.* :—

(1) The Bank receives dividends by power of attorney or otherwise for all persons having drawing accounts at the Bank.

(2) Cheques may be drawn for £5 and upwards instead of £10 as heretofore.

(3) Cash boxes taken in, contents unknown, for such parties as keep accounts at the Bank.

(4) Bank notes are paid at the counter instead of drawing tickets for them as heretofore.

(5) Cheques on city bankers, paid in by 3 P.M., are received and passed to account the same evening.

(6) Bills of exchange, payable at the Bank, are paid with or without advice, heretofore with advice only.

(7) Notes of country bankers, payable in London, are sent out the same day for payment.

(8) Cheques are given out in books, and not in sheets as heretofore.

It may be observed that cheques on clearing bankers can now be received until 4 P.M.

CHAPTER VIII.

JOINT-STOCK BANKING.

WITH the development of trade and commerce, a need was experienced for additional banking facilities ; the failure of many private bankers was the means of bringing into prominence the joint-stock principle as applied to banking. No doubt the large number of failures (about 1,000 banks), from 1793 to 1818, seemed somewhat alarming ; but we must consider that the period was a critical one in the history of the country, and if the joint-stock principles had been utilised we think that the effect would have been the same. In fact, the first joint-stock banks constituted were not more successful than their rivals. Again, it was supposed that the business of banking was very profitable, and consequently the joint-stock principle for such purposes would be advantageous.

It was also discovered that the Bank of England's Charter stated " only borrowing or owing money on their bills or notes " was prevented, therefore it was quite possible for a joint-stock bank to be formed to receive money on *deposit*.

Mr. Joplin stated in 1823 : " That public banks have not hitherto existed, more especially in London and Lancashire, seems to have risen from the want of a proper knowledge of the principle of banking rather than from the

Charter of the Bank of England, *which I find does not prevent public banks for the deposit of capital from being established* ”.

An attempt was made to induce the Bank of England to give up its monopoly of exclusive banking, but that institution would not, however, agree to the proposition. The Government, nevertheless, in 1826 passed an Act allowing joint-stock banks to be formed beyond sixty-five miles of London.

The Act states : (1) “ That banks of an unlimited number of partners may be formed, provided that they shall not have any house of business in London, or at any place within sixty-five miles thereof.

(2) “ No such banking company was to issue or reissue either directly or indirectly within the prescribed distance any bill or note payable to bearer on demand or any bank post bill, nor draw upon its London agents any bill of exchange payable on demand, or for any less sum than £50, but they might draw any bill for any sum of £50 and upwards in London or elsewhere at any period after date or after sight.

(3) “ Banks of an unlimited number of partners may issue notes, but they must deliver at the Stamp Office an account containing the names of the firm, etc.

(4) “ Co-partnerships may sue or be sued in the names of their public officers.

(5) “ The Governor and Company of the Bank of England may empower agents to carry on banking business at any place in England.”

Banks were very soon formed in various parts of the country ; so that in 1826 there were joint-stock establishments at—

Liverpool.		Darlington.
Manchester, and two branches.		Lancaster, and three branches
Manchester and	} and nine branches.	Whitehaven.
Liverpool,		Carlisle, and seven branches.
Birmingham.		Leicester.
Wolverhampton.		Norwich, and nine branches.
Sheffield.		Stamford.
Barnsley.		Spalding.
Bradford.		Gloucester.
Halifax.		Langport, and fourteen branches.
Huddersfield.		Plymouth.
Knaresboro'.		Devonport.
York.		

Unfortunately the supply of joint-stock banks was far greater than the demand ; a few years later a large number of them failed through lending money in a reckless manner.

People began to look upon them with distrust. Lord Overstone observed in 1832 : “ I think the joint-stock banks are deficient in everything requisite for the conduct of banking business except extended responsibility. The banking business requires peculiarly persons attentive to all its details, constantly, daily, hourly watchful of every transaction, much more than mercantile or trading business. Joint-stock banking, of course, obliges to act through agents and not by a principal, and therefore under the restraint of general rules cannot be guided by so nice a reference to degrees of difference in the character of responsibility of parties, nor can they undertake to regulate the assistance to be granted to concerns under temporary embarrassments by so accurate a reference to the circumstances, favourable or unfavourable, of each case.”

These remarks of Lord Overstone were no doubt quite correct with reference to loans on personal security, but when banks were formed in London it was impossible to carry on business on these principles, consequent on the rapid development of trade in the Metropolis. A London

bank cannot know the position and standing of each individual in the same manner as the country banker; the information as to means and character is not so comprehensive.

In the year 1833 banks were allowed to issue notes above £50 payable on demand in London. They were required by this Act to keep a weekly account of their notes in circulation, and make a return of the amount to the Commissioner of Stamps. On the renewal of the Charter of the Bank of England in 1833, the Government would not amend it in order to prevent joint-stock banks being formed in London; but inserted a clause allowing joint-stock banks in London, provided they did not borrow or take up in England any sum or sums of money on their bills or notes payable on demand, or at any less time than six months from the borrowing thereof. The Act also stated that no partnership exceeding six persons shall make or issue in London, or within sixty-five miles thereof, any bill of exchange or promissory note or engagement for the payment of money on demand, or upon which any person holding the same may obtain payment on demand.

This Act also stated that an account of the bullion, notes in circulation and deposits in the Bank of England shall be transmitted weekly to the Chancellor of the Exchequer.

Joint-stock banks were soon formed in London after the passing of this Act. The London and Westminster began business in 1834, the Union Bank of London in 1839, the London and County in 1836, and the Commercial Bank of London in 1840.

The London and Westminster Bank in its prospectus stated that it would receive current accounts on the same terms as other London bankers, but that no interest would be allowed on such accounts. Deposit receipts

would be issued for sums from £10 to £1,000, bearing interest at the rate of 2 per cent. per annum, but if the amount should be withdrawn within three months, no interest would be allowed. Parties respectably introduced, not having an account at the bank, might, nevertheless, have their bills discounted or loans granted them on approved securities. The bank would act as agent to joint-stock banks, private bankers, and other parties residing at a distance. Persons who should require letters of credit to any part of the United Kingdom, the Continent of Europe, or other parts of the world, might obtain the same.

The joint-stock banks formed in London had to contend with great difficulties; these banks existed only in the form of an ordinary common law partnership; consequently in an action all the shareholders had to join. This was not remedied until the year 1844. The London and Westminster Bank applied for a bill to sue and be sued in the name of its Chairman, but this was refused; in consequence of this, all the London joint-stock banks were sued in the names of trustees.

The new banks were looked upon with suspicion, and it was thought they would not succeed; consequently, the Bank of England refused to open accounts for them in its books, and the private bankers would not admit them to the Clearing House.

The Act which permitted their formation did not allow them to accept bills at a less date than six months. However, in 1838 an Act was passed which allowed "a banking company to sue and be sued by any of its members exactly as if they were separate individuals". Prior to the passing of this Act, a shareholder in two different banks was unable to take proceedings. In the year 1840

the provisions of the Act were also extended to criminal cases.

An Act, passed in 1856, allowed directors in banking companies to be eligible for re-election when their term of office expired.

In the year 1857 joint-stock banks were bound to register themselves in the same manner as other companies; this Act also allowed the number of partners in private banks to be increased to ten. A great change in the constitution of banks was made in 1858, when banking companies were allowed to be formed with limited liability; consequently, all banks constituted after that date were on this principle.

This was in many ways beneficial, because shareholders as a rule like to know the extent of their liability. For example, if a bank is unlimited there is a tendency for its shareholders to consist of a class with small capital. It has been suggested that directors of banks should be liable to an unlimited extent in order to give a greater protection to shareholders, but we think there would be some difficulty in obtaining directors of high repute if such conditions were imposed. If a bank is registered as a limited liability company, it is still desirable that a portion of its capital should remain uncalled, as a protection for its depositors.

Banks may be formed by royal charter or letters patent. The liability of members is usually limited to the amount of their respective shares. The charter is generally for a limited period, but renewable, and the liability of some banks thus constituted extends to an amount equal to the capital.

The following table will show the various dates at which the joint-stock banks were formed in this country :—

From 1826-30 =	10
1831-35 =	28
1836-40 =	34
1841-45 =	3
1846-50 =	0
1851-55 =	1
1856-60 =	0
1861-65 =	26
1866-70 =	5
1871-74 =	11
	<hr/>
	118

These banks are divided as follows :—

	1845.	1860.	1865.	1870.	1875.	1895.	1902.
Purely London Banks	4	7	11	12	12	5	3
London and Provincial Banks	1	2	9	8	7	12	20
Provincial Banks	—	85	93	92	99	82	44
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
	5	94	113	112	118	99	67

The great reduction of banks in recent years is due to amalgamation of various institutions, both private and joint-stock, which is the leading feature of modern banking.

Some of these banks have a large number of branches ; the number of bank offices having largely increased in recent years.

Thus in 1851 = 962 offices = 1 office to 18,700 inhabitants.

1854 =	—	„	1	„	16,500	„
1870 =	1,651	„	1	„	13,500	„
1875 =	1,885	„	1	„	12,600	„
1878 =	2,195	„	—	„	—	—
1883 =	2,381	„	1	„	11,135	„
1903 =	—	„	1	„	6,642	„

From 1876 to 1901 no less than 3,124 new banking offices were opened in England and Wales.

The following table shows the increase in joint-stock banks in the years 1844, 1894 and 1902 :—

	1844.	1894	1902.
Joint-stock Banks, head offices .	106	99	67
„ „ branches .	493	2,577	4,230
	<hr/> 604	<hr/> 2,676	<hr/> 4,297

These tables show the enormous growth of joint-stock banks in this country.

Mr. Gilbert stated that the capital of a bank should be at least one-third of its liabilities; but when we see banks paying large dividends, say from 15 per cent. to 20 per cent. and upwards, it may be assumed that the capital is small in proportion to their liabilities. The Scotch banks show a proportion of about 12·70, but the English banks is somewhat smaller, *viz.*, 10·70.

In the year 1903 there were sixty-seven banks, with the enormous capital of £62,840,000; these banks had accumulated, partly out of profits, as reserve, the sum of £37,232,000.

The increase in the banking capital of the United Kingdom in 1903 was £1,896,000.

For six years ending 1901 the banks of England and Wales have increased their reserves by £7,550,000, which is satisfactory, because it shows that the banks are strengthening their position against increasing liabilities. In the year 1878 fully £1,000,000 of capital was lost by the failures of the City of Glasgow and West of England Banks.

The prospectus of the London and Westminster Bank, which we have quoted, stated that money would be taken on deposit and interest allowed. Although this is the usual custom amongst banks of the present day, yet the early bankers considered it was not desirable for them to find investments for the capital of those who were not their clients. No doubt the doctrine was possibly sound, because in times of distrust the depositor is the first to withdraw his capital. The banks in the present day have

become, as it were, huge savings banks, and, with large reserves, are in a better position to stand any withdrawal of depositors' money.

The competition between bankers, bill brokers and foreign and colonial banks in London has made it difficult at times to employ deposit money at a profit.

If money "at call" is $\frac{1}{2}$ per cent., and first-class paper is discounted at $\frac{3}{4}$ per cent., it is a question whether bankers can afford to pay even $\frac{1}{2}$ per cent. on deposits. It was stated some time ago in a London journal that when call money was $\frac{1}{4}$ per cent. it scarcely paid for the ink, paper and labour in making the necessary entries. We must not forget to include the working expenses before ascertaining the amount of interest which a banker can afford to pay on deposits.

In times of distrust the depositor is generally the first one to demand his money, and that was the principal reason why the private bankers did not encourage deposit banking. The Australian banking crisis showed that the depositors were the first to take alarm, so that it is important to keep large reserves against deposits.

The growth of deposits and current accounts of some of the London banks is shown in the following table:—

	1844	1874.	1903.
London and Westminster .	£2,697,000	£30,020,000	£26,652,000
London Joint-Stock Bank .	2,245,000	16,000,000	18,284,000
Union of London * . . .	1,591,000	14,120,000	28,445,000
Commercial Bank of London .	240,000	—	—
London and County . . .	1,231,000	20,072,000	44,142,000
London City and Midland * .	—	3,290,000	44,165,000

or an increase of 10·10 per cent.

The following table shows the increase in the deposits,

* The recent amalgamation of private banks has been the cause of the large increase in deposits.

etc., of the principal joint-stock banks in London from 1849 to 1859 :—

When Formed.	Capital.	Bank. £	Year.	Current and Deposit Accounts. £	Increase Per Cent.	Guarantee and Reserve Fund. £	Proportion of Capital and Guarantee to Deposits.	Dividends and Bonus. Per Cent.
1834	1,000,000	London and Westmr.	1849	3,680,000		108,000		6
			1854	7,177,000	95	134,000	16	14
			1859	11,115,000	55	200,000	10	18
1836	600,000	Joint	1849	2,792,000		132,000		9 $\frac{3}{4}$
			1854	6,161,000	120	156,000	12	25
			1859	9,556,000	55	229,000	9	18
1836	500,000	London and County	1849	1,675,000		28,000		6
			1854	3,779,000	126	62,000	15	12
			1859	4,975,000	32	105,000	12	11
1839	720,000	Union	1849	2,835,000		50,000		6
			1854	7,031,000	148	50,000	11	15
			1859	9,318,000	33	95,000	9	15
1855	300,000	City Bk.	1859	2,223,000		33,000	15	6

The deposits in the London joint-stock banks sometimes exhibit a decrease during a period of distrust. This is shown by the following table, in 1878, when there were several bank failures :—

CASH DEPOSITS.

	Dec. 31, 1878. £	June 30, 1878. £	June 30, 1871. £
London and Westminster .	21,490,000	26,760,000	22,770,000
Joint	13,850,000	14,680,000	14,610,000
Union	12,400,000	12,540,000	12,710,000
City	2,870,000	3,920,000	2,360,000
Alliance	1,810,000	2,430,000	1,600,000
Imperial	1,620,000	2,270,000	2,230,000
Consolidated	2,560,000	2,960,000	2,450,000
Central	960,000	1,140,000	570,000
Metropolitan	—	320,000	590,000
London and South-Western	1,560,000	1,570,000	570,000
Totals	£59,120,000	£68,590,000	£60,460,000

The paid-up capital and reserve of these London banks amounted to £10,370,000 on 31st December, 1878, and £10,490,000 on 30th June, 1878.

LONDON BANKS—CASH DEPOSITS, 30TH JUNE, 1903.

London and Westminster	£26,652,000
National	11,211,000
London Joint-Stock Bank	18,284,000
London and County	44,142,000
London City and Midland	44,165,000
Union of London and Smiths Bank	28,445,000
London and South-Western	13,220,000
Parr's Bank	27,610,000
London and Provincial Bank	12,849,000
Martin's	3,338,000
Barclay & Co., Limited	36,168,000
Capital and Counties	26,351,000
Glyn, Mills, Currie & Co.	13,619,000
Lloyds	56,158,000
National Provincial Bank	50,948,000
Williams Deacon's Bank	11,691,000
	<hr/>
	£124,851,000

Unfortunately it is impossible to give the same details showing the progress of the joint-stock country banks, since a large number of them did not publish balance sheets until quite recently; but in order to show the rapid progress of English banking, we give the following statement of 100 banks, *viz.* :—

100 BANKS, ENGLAND AND WALES.

1883	Deposits	£286,100,000
	Cash and money at call	79,550,000
1895	Deposits	485,277,000
	Cash and money at call	144,163,000

69 BANKS, ENGLAND AND WALES.

1903	Deposits	£645,000,000
	Cash and money at call	152,000,000

Comparing 1869 with 1903 we find that the banks paying between 5 per cent. and 10 per cent. were more in 1869 than at the present time. The profits have increased

with the greater activity in trade; it is satisfactory to note that the reserves have increased more than the profits.

Total of reserves . . . 1869 = £12,815,000
 1878 = 21,297,000
 1903 = 37,000,000

	1869		1878.		1903.	
	No.	Capital.	No.	Capital.	No.	Capital.
Banks paying 20 per cent. and upwards	15	£ 5,302,000	18	£ 5,828,000	8	£ 7,159,000
Banks paying 15 to 20 per cent.	20	5,439,000	28	12,684,000	18	21,050,000
„ „ 10 to 15 „	36	14,057,000	44	21,916,000	20	28,638,000
„ „ 5 to 10 „	36	14,182,000	15	6,620,000	14	4,710,000
„ „ less than 5 „	3	1,350,000	4	564,000	4	176,000
Banks	110	40,330,000	109	47,612,000	64	61,733,000

The great accumulation of capital in joint-stock banks has taken place in recent years; it is, however, necessary that reserves should be strengthened in order to meet the yearly growth of liabilities.

It is desirable that a uniform balance sheet should be adopted by all the joint-stock banks in England and Wales, since it would be advantageous, not only to the community, but also to the banks themselves, as from comparison valuable information may be obtained. Any defects as to the management of other institutions might possibly be discovered and remedied for the benefit of depositors and shareholders. In recent years the principal banks have issued monthly a statement of the amount of cash held, which enables us somewhat to ascertain what cash reserves are held against deposits and other liabilities.

CHAPTER IX.

THE PRIVATE BANKERS.

WE have already referred to the private bankers who founded our banking system, and it must not be forgotten that business was carried on by them during critical periods in the history of the country. A great number were men of high reputation, and, as bankers, they rendered considerable assistance to the Government at times when the finances of the country were in a critical condition. They also contributed largely towards promoting a uniformity of banking practice; legislation on a variety of subjects appertaining to banking was principally due to their efforts.

It might be observed that when the first joint-stock banks were formed it was necessary to obtain officials from the private banks; consequently, there was a continuity in the old methods of business. The cause of their diminution is due to a variety of causes; some have become extinct in consequence of the death of partners; whilst many have amalgamated with other banking institutions. This latter process, which is the essential feature of modern banking, has also eliminated some of the smaller joint-stock banks. The tendency of the present day is in favour of great combinations, but whether it will be successful, as applied to banking, is at present somewhat difficult to judge.

Quite recently we have had an amalgamation of various private banks, constituted as a joint-stock company, but carrying on business under the old traditional system of

private banking. With regard to those who remain, we might observe that they are well-known bankers, and have an intimate knowledge of their profession. In recent years a great number have published balance sheets; the figures show that their capital and reserves form an adequate fund for banking purposes.

The following tables show the number of private banks in existence from 1808 until the present time :—

1808 = 600
 1810 = 721
 1844 = 335 and 93 branch offices.
 1875 = 251
 1894 = 101 and 464 „
 1903 = 42

	1860.	1865.	1870.	1875.	1894.	1903.
Purely London Bankers .	53	46	47	55	21	11
Provincial „ .	239	211	207	196	80	31
	292	257	254	251	101	42

In the year 1878 four private bankers stopped payment, thus still reducing their number.

LONDON PRIVATE BANKS.

1810 = 40 Clearing House.
 1845 = 26 „ „
 1858 = { 25 Clearing Bankers.
 { 22 Non-Clearing Bankers.
 1866 = { 14 Clearing Bankers.
 { 18 Non-Clearing Bankers.
 1872 = { 13 Clearing Bankers.
 { 17 Non-Clearing Bankers.
 1878 = { 12 Clearing Bankers.
 { 18 Non-Clearing Bankers.
 1895 = { 5 Clearing Bankers.
 { 16 Non-Clearing Bankers.
 1903 = { 1 Clearing Banker.
 { 11 Non-Clearing Bankers.

The deposits held at the disposal of the London private bankers were estimated in 1834 at £29,500,000, of which the sum of £3,000,000 belonged to country bankers. Mr. Dun estimated in 1876 that the money lodged with such London institutions amounted to £80,000,000, and with country private bankers to £93,500,000. In 1903 seventeen private banks held £50,000,000 of deposits.

CHAPTER X.

BANKING IN SCOTLAND.

THE Bank of Scotland was the first institution of its kind formed in that country, and obtained an Act from the Scotch Parliament on 17th July, 1695, which authorised the Crown to grant a Charter of Incorporation. Unlike the Bank of England, it was not connected with the State, although possessing a monopoly of banking for twenty-one years; at first money was not received on deposit, and profits depended entirely upon the note circulation.

The next bank formed was the Royal Bank of 1727, being the lineal descendant of the Darien Company. Its promoters complained that the rival institution, *viz.*, the Bank of Scotland, charged too high a rate of interest for loans, and that it was hostile to the House of Hanover. It was also stated that the Bank of Scotland was very exacting with regard to the securities required, and loans on its own stock were not allowed.

In consequence of these charges the monopoly of the Bank of Scotland was abolished.

The British Linen Company was established in 1746 for carrying on the business of linen manufacturers as well as of banking; but the former business was, however, soon relinquished.

The next institution that came into existence was the Ayr Bank, and its promoters supposed that notes could

be issued to an unlimited extent; but, fortunately, this popular delusion was soon dissipated, because, after issuing £800,000 of paper money, this bank was unable to pay the notes on demand. In the year 1772 it stopped payment; the effect of its suspension was so great that only three of the then existing private banks survived the panic.

There are no private banks in Scotland, but there were eight in existence in 1819.

The following table shows the increase in the number of banks and branches :—

1819 = 30 chief offices and 97 branches.	
1830 = 27	145
1845 = 20	376
1864 = 13	591
1878 = 12	940
1894 = 10	1,008
1900 = 10	1,077

The number of offices in proportion to the inhabitants is larger in Scotland than in England or Ireland. Thus :—

No. of offices in 1826 =	167 or 1 to every	13,170 inhabitants.
„ „ 1841 =	380 „ „	6,600 „
„ „ 1856 =	585 „ „	5,230 „
„ „ 1872 =	790 „ „	4,250 „
„ „ 1883 =	898 „ „	4,260 „
„ „ 1901 =	1,087 „ „	4,114 „

Although the facilities for banking are greater in Scotland than England, yet, on the other hand, working expenses must have the effect of diminishing profits.

The great success of the Scotch system is supposed to be due to three circumstances, *viz.*: 1st, banking in that country was not originally a monopoly, although the privilege of note issue made it so at a later date; 2nd, it was treated as an ordinary business in which the State was only indirectly concerned; and 3rd, the only restrictions were that the banks should confine themselves to banking.

The Act of 1845, relating to Scotland, stated that no

new bank of issue should be formed, and this practically prevented new banks opening, because the issue of notes is an essential part of Scotch banking. Since the Act was passed, seven banks of issue have ceased to exist, *viz.*, Aberdeen Bank, Dundee Bank, Eastern Bank, Edinburgh and Glasgow Bank, Perth Bank, Western Bank, and City of Glasgow Bank.

We have already noticed that the issue of £1 notes was allowed by the Act of 1845, and the circulation has far exceeded the authorised limit. This Act also prevented other banks from being formed, consequently we have large institutions with correspondingly great liabilities. If at any time failures should occur in the country, the effect may possibly be disastrous. No doubt there would have been more banking institutions in Scotland if the existing banks were not practically in possession of a monopoly.

Another feature of Scotch banking is the system of deposits; small amounts are received, and consequently the banks assume somewhat the character of savings banks. The great prosperity of the people has been attributed to such banking facilities.

This concentration of capital at places where required must materially benefit any country, and consequently increase its wealth.

In Scotland there are more bank shareholders in proportion to the inhabitants than in England or Ireland, showing that the community have great confidence in their banking institutions.

The Scotch are thus more directly interested in the success of their institutions, consequently, in times of panic and commercial distrust, they do not lose confidence; so that sudden withdrawals of deposits have not taken place.

The system of cash credits is another peculiar feature of Scotch banking ; any person who can obtain two sureties willing to give a bond of indemnity is allowed to draw against the amount placed to his credit at the bank. The sureties have a right to inspect the bank books in order to see that the account is in strict accordance with the bond.

The progress of money lodged has not been so rapid as in England. Thus :—

	£
1826 =	21,000,000
1841 =	27,000,000
1844 =	33,192,000
1855 =	43,271,000
1865 =	56,185,000
1875 =	78,405,000
1895 =	93,489,068
1903 =	106,437,000

The following is a list of the banks now in existence : --

		Paid-up Capital.	Reserve.
		£	£
Bank of Scotland . . .	1695	1,250,000	875,000
Royal Bank of Scotland . .	1727	2,000,000	900,724
British Linen Company . .	1746	1,250,000	1,650,000
Commercial Bank . . .	1810	1,000,000	1,000,000
National Bank of Scotland .	1825	1,000,000	1,030,000
Union Bank of Scotland . .	1830	1,000,000	785,000
Clydesdale	1838	1,000,000	700,000
Town and County, Aberdeen	1825	252,000	154,000
North of Scotland . . .	1836	400,000	167,500
Caledonian	1838	150,000	51,000
Mercantile Bank of Scotland		14,070	3,000
		<hr/>	<hr/>
		£9,316,070	£7,316,224

The Bank of Scotland, the Royal, and the British Linen Company are chartered banks, but the remainder became limited after the failure of the City of Glasgow Bank ; it is presumed that only the corporate property of the chartered banks would be liable for debt.

The total liabilities of these banks amount collectively

to £137,568,000, their cash and Government securities to £58,300,000, and the ratio of cash in hand and money at call is about $17\frac{1}{2}$ per cent.

The note circulation of the Scotch banks is equal to about 50 per cent. of their capital and reserve fund.

That the Scotch people are prudent, saving and industrious is shown by the cash deposits, which amounted a few years ago to £90 per head of the adult male population; this is a far greater proportion than in England or Ireland.

The Scotch banks are to be commended for publishing a complete balance sheet, which enables us to show clearly the progress of banking in that country :—

11 Banks.

LIABILITIES.

	Deposits.	Notes.	Acceptances and Drafts.	Total Liabilities.
	£	£	£	£
1865	57,140,000	4,986,946	2,668,881	64,796,247
1869	63,820,000	5,390,947	4,296,319	73,508,077
1894 (10 banks). }	93,489,068	6,733,523	2,981,638	120,337,697
1903	106,437,000	8,005,000	3,366,000	137,568,000

ASSETS.

	Banking Advances.	Stocks and other Secs.	Banking Premises.	Reserves.	Total Assets.
	£	£	£	£	£
1865	54,878,548	3,925,530	1,091,862	17,297,925	77,193,871
1869	61,095,648	4,037,530	1,187,114	20,114,153	86,434,559
1894 (10 banks). }	60,743,952	31,068,042	6,359,933	22,165,770	120,337,697
1903	71,616,000	32,439,000	7,632,000	25,881,000	137,568,000

The following is an abstract of balance sheets from 1870 to 1903 :—

	Due to Proprietors.		Due to Public.			Assets.		Total Assets.	Net Profits.
	Capital.	Reserve.	Circ.	Deposits.	Accepts.	Cash, etc.	Disc'ts.		
	£	£	£	£	£	£	£	£	£
1870-71	8·77*	3·51	5·85	59·60	4·11	23·16	59·79	81·95	1,109
1874-75	9·00	3·46	7·46	74·27	5·05	27·62	72·68	100·30	1,284
1875-76	9·00	4·49	6·86	74·37	5·72	27·49	73·38	100·87	1,275
1876-77	9·00	4·98	6·84	73·83	6·24	28·95	72·65	101·30	1,287
1894 (10 banks.)	9·00	5·71	6·73	93·48	2·98	22·16	60·74	120·33	936
1903	9·31	7·40	8·00	106·40	3·36	25·88	71·61	137·56	1,178

These tables show—

(1) There has been an increase in the note circulation of £2,200,000.

(2) An increase of deposits in nine years of £13,000,000.

(3) There has been a decrease in acceptances in thirty-four years from £4,110,000 to £3,366,000.

(4) The net profits of the Scotch banks in recent years have considerably increased.

There was a decrease in deposits in consequence of the failure of the City of Glasgow Bank, which is shown from the following statement :—

May 18, 1878	.	.	.	.	.	£78,000,000
October 19, 1878	.	.	.	.	.	78,000,000
May 17, 1879	.	.	.	.	.	67,000,000

The latest reports, however, show that deposits are steadily increasing.

Another feature of Scotch banking was the allowance of interest on current accounts, which somewhat differs from the procedure of the majority of English banks, but recently this system has been abandoned. Interest was

* 0·000's omitted from columns 2 to 9 and 000's from column 10, thus £8·77 = £8·770·000.

formerly allowed on current account by some of the English banks, but increasing competition made it unprofitable.

In 1863 the Scotch banks fixed the following rates, *viz.* :—

Daily balances from $1\frac{1}{2}$ to 4 per cent.

Minimum balances from 2 to $4\frac{1}{2}$ per cent.

The interest for advances from 1822 to 1864 was never below 4 per cent. :—

1847 = $5\frac{1}{2}$ per cent.

1863 = 7 per cent.

1856 = 6 per cent.

1864 = 8 and 9 per cent.

1857 = $6\frac{1}{2}$ per cent.

An account of the progress of the Scotch banks would be incomplete without reference to the great banking disasters in 1857 and 1878.

It was thought that banking in Scotland was safe and prosperous; in fact, some believed that the failure of banking institutions in that country was impossible, but this delusion was dispelled by the great failures of 1857 and 1878. These great disasters showed that Scotch bank directors could act in a reckless manner like other individuals. The failures of the Western Bank of Scotland in 1857, and the City of Glasgow Bank in 1878, were very similar in character. In 1857 the Western Bank lent to four or five private firms a sum equal to its capital, and had also an agency in New York, where a large proportion of its deposits was sent to support all kinds of speculation. When however speculation in America experienced a sudden check, the Western Bank found itself in the possession of a large amount of worthless securities, and that bank, being unable to meet its liabilities, was obliged to close its doors. It was ascertained that the capital of £1,500,000, the reserve fund of £227,000, and £916,864 6s. 8d. in addition was lost. The failure of such a large institution caused a run upon

all the others, but they gave credit and paid the notes of the bankrupt bank, which soon had the desired effect.

The City of Glasgow Bank suspended payment for a short time in 1857, but if subsequent events were known, it would have been advantageous if its doors had not been opened. The failure of this bank in 1878 was very disastrous, because English banking institutions as well as Scotch banks felt the effects of the suspension.

Shareholders in such institutions saw how easy it was to deceive; the accounts of the Glasgow Bank had been falsified from the year 1873. The liabilities were £2,000,000 more than stated in the balance of 5th June, 1878, whilst the assets were nearly £5,000,000 less, namely :—

Bills of Exchange	£2,400,000 less than stated.
Advances on heritable property	50,000 „ „
Cash on hand	400,000 „ „
Government stocks, etc.	1,700,000 „ „
	<hr/>
	£4,550,000

Deducting the capital and reserve, £5,190,983 11s. 3d. had to be provided for by the shareholders.

The Act of 1845 stated that the excess in the circulation above the authorised issue should be represented by gold, but for some time the Glasgow Bank had made false returns to the Government, since it did not hold the requisite amount.

No doubt Sir Robert Peel intended that the gold held should be a cover for the note issue, but it seems that the Act of 1845 was a failure in this respect. The other banks promptly met the disaster by paying the notes of the Glasgow Bank, and also giving every facility to those who had money locked up in that bank. The business of the City of Glasgow Bank had been badly managed, the directors having lent large sums of money

to their own firms ; no less than £5,800,000 was advanced to four commercial houses in which they were interested. They also supported undertakings which every day were becoming more insolvent, and issued bills supposed to be drawn in Melbourne, but in reality at Glasgow. As a last resource they invested large sums of money upon land in Australia and New Zealand, thus hoping to retrieve their position. It is important to remember that when the City of Glasgow Bank's acceptances were refused in the London Money Market, the bank was in reality doomed, so that its doors were closed within a week. This shows the danger that may arise from a bank having a large amount of acceptances in the market. Although this great failure depreciated the value of bank shares, and caused a large withdrawal of deposits, yet it was not without its advantages, since it was the means of clearing away insolvent houses.

Banking was brought prominently before the public, and many important questions relating to that subject were discussed with a view to certain reforms being carried out.

The opening of London offices by Scotch banks was the cause of some comment in the country.

The following are now represented in the Metropolis :—

Bank of Scotland	opened in 1868
Royal Bank of Scotland	„ 1875
British Linen Company Bank	„ 1877
National Bank of Scotland	„ 1864
Union Bank of Scotland	„ 1878
Clydesdale Bank	„ 1874
Commercial Bank of Scotland	„ 1883

It has been stated that the Scotch banks have not shown their usual prudence by opening offices in London for the following reasons :—

(1) They had in their own country a prosperous and

sound business, with profits and dividends considerably increasing.

(2) That the scheme of opening London offices is a departure of the most marked kind from the maxims which have hitherto guided them.

(3) That the Scotch banks, assuming responsibilities of London institutions, must remodel their reserve funds.

The *Scotsman* of March, 1878, stated " that the experiment of raising deposits in Scotland and using them in London will be watched with interest ".

Another point in connection with the opening of London offices was the large increase in the acceptances of those banks—transactions which must always be carried on with great caution. In times of commercial distrust the credit of any bank may possibly be affected by the amount of its bills circulating in the market, and securities held as cover may depreciate in value.

The following table shows the increase in the acceptances of Scotch banks from 1870 to 1877 :—

	1870-71.	1876-77.	Increase.
	£	£	£
Two banks with London offices .	2,220,000	3,620,000	1,400,000
City of Glasgow Bank . . .	770,000	1,350,000	580,000
	<hr/>	<hr/>	<hr/>
	£3,000,000	£4,970,000	£1,980,000
Five other banks	1,120,000	1,770,000	650,000
	<hr/>	<hr/>	<hr/>
	£4,120,000	£6,740,000	£2,630,000

In 1876-77 these acceptances were equal to one-fourth of the total acceptances of the London joint-stock banks, but there has been a great decrease in recent years, the present amount being £3,366,000. It seems an anomaly that Scotch banks of issue can open branches in London, whereas English country banks are required to forfeit their note circulation on doing so.

The National Provincial Bank gave up its issue on

opening in London, losing thereby £10,000 per annum. Besides this, the Scotch Act of 1875 gave the banks considerable privileges, which practically secured for them the monopoly of banking in that country.

Lord Goschen in 1875 introduced a bill to prevent the Scotch banks from opening in London, but this met with considerable opposition and was abandoned; a clause was inserted in the Banking Bill of 1878, stating that all banks opening in London should forfeit the right of issuing notes, but this was struck out.

The dividends paid by the Scotch banks in 1869 were in comparison with the English banks in a lower class, the reason apparently being the large paid-up capital. If we compare 1869 with 1903 we find that the Scotch banks had considerably increased their dividends, but the period from 1878 to 1894 shows a decrease:—

	1869.	1878.	1894.	1903.
Bank of Scotland	12	14	12	14
British Linen Company	13	14	15	20
Caledonian Banking Company	10	14	8	8
Clydesdale	10	14	10	12
Commercial Bank	13	15	15	20
National Bank	12	15	15	20
North of Scotland	10	13 $\frac{3}{4}$	6 $\frac{1}{4}$	8 $\frac{3}{4}$
Union Bank of Scotland	10	13	10	13
City of Glasgow	8	11 $\frac{1}{2}$	—	—
Royal Bank of Scotland	8	9 $\frac{1}{2}$	8	10
Town and County Bank	—	—	—	12 $\frac{1}{2}$
Mercantile Bank of Scotland	—	—	—	4

The Scotch banks in 1876 agreed to the following charges:—

(1) Interest on money lodged and on advances and discounts to be fixed at meetings of the banks to be held at Edinburgh.

(2) In addition to the discount a commission of 1s. 3d. per cent. is charged on bills payable in Scotland; on bills

payable in London no commission is charged, but elsewhere in England and Wales, 2s. 6d. per cent.

(3) Other fixed charges are made for negotiating documents payable on demand, for granting drafts, making transfers, etc.

With regard to the London offices it must be remembered that the Metropolis is the centre for the world's commerce, and banks with large amounts of deposit money must utilise the same at a profit. The business can possibly be transacted on better terms than through the medium of an agent; the growth of business has also caused various foreign banks to open London offices in order to minimise the cost of banking operations.

CHAPTER XI.

BANKING IN IRELAND.

BANKING in Ireland somewhat resembles the English system, because in the earlier stages of its history there were a large number of private banks, but in 1783 the monopoly of joint-stock banking was given to one institution, *viz.*, the Bank of Ireland. The charter of this bank prevented partnerships of more than six persons from being formed, and consequently there existed a large number of private banks without sufficient capital, and when many of these failed the result was disastrous to the trade of the country.

Ireland has suffered considerably from political events, which naturally prevented the development of banking, which is based upon confidence as well as the industrial pursuits of the people.

A need was felt for a central banking institution, and the success of the Banks of England and Scotland stimulated the efforts of the people for the establishment of institutions which should tend to develop the resources of the people.

The privileges of joint-stock banking were, however, granted on the understanding that the capital should be lent to the Government. The first amount raised was £600,000, Irish Currency Act, 21 & 22 George III., and in 1791, on the renewal of the charter, the capital was increased to £1,000,000.

The following amounts were added, *viz.*:—

1797	£500,000
1808	1,250,000
1821	500,000

The total amount of capital was thus £3,000,000 Irish, equal to £2,769,230 15s. 5d. sterling money of Great Britain.

In the year 1824 the Bank of Ireland surrendered its monopoly of joint-stock banking beyond sixty-five miles of Dublin, but it was not until the year 1845 that all the restrictions upon banks having more than six partners were abolished. From 1845 any joint-stock bank could have offices in Dublin, but no new bank was allowed to issue bank notes.

BANK OF IRELAND—DEBT.

	Irish Currency.		English Currency.	
	£		£	s. d.
1782	600,000	=	553,846	3 1
1797	500,000	=	461,538	9 3
1808	1,250,000	=	1,153,846	3 1
1821	500,000	=	461,538	9 3
	£2,850,000		£2,630,769	4 8

As already stated, there were a large number of private banks in existence during the earlier periods of Irish banking. The private bankers carried on business as goldsmiths, or other trades, and issued notes against the deposit of money. These promissory notes were legally recognised in the year 1709, when it was enacted that they were assignable and transferable by endorsement.

In 1735 five private banks were carrying on business in Dublin, *viz.*, James Swift & Co., Hugh Henry, Nuttall & McGuire, La Touche & Kane, and Joseph Fade & Co.

There were about fifty private banks existing in 1804, but in 1815 they were reduced to thirty-one, and according to the *Post Office London Directory* of 1817 the names of only twenty-one appear. At the present time there

are only two private banks, *viz.*, Messrs. Boyle, Low, Murray & Co., and Messrs. Guinness, Mahon & Co., but these firms do not confine their business entirely to banking.

* The banks which failed after the Bank Act of 1824-25 were as follows :—

	Established.	Failed.
Agricultural Bank of Ireland	1834	1841
Southern Bank of Ireland	1837	1837
Tipperary Joint-Stock Bank	1838	1856
Munster Bank	1864	1885

The following banks transferred their business to other institutions, *viz.* :—

	Established.	Transferred to
London and Dublin Bank	1843	1848 National Bank.
Union Bank of Ireland	1862	1868 { Munster Bank.
English and Irish Bank	1863	1864 { Hibernian Bank.
European Bank }	1864	1865 European Bank.
Dublin Branch }		Munster Bank.

In the year 1825 an Act was passed for the purpose of assimilating the currency of Ireland with that of England. Prior to this date an English shilling was valued at 13d., and an English sovereign at £1 1s. 8d.

We have already noticed that the Act of 1845 relating to the note issue was similar to Scotland, where the issue of £1 was allowed, and also that no new banks were permitted to issue notes.

The banking institutions now in existence are as follows, *viz.*, the Bank of Ireland, incorporated by charter; in fact, somewhat similar to the Bank of England; it has the privilege of issuing notes, and keeps the Government accounts. The interest on the capital lent to the Government was $3\frac{1}{2}$ per cent. in 1845, but subsequently reduced in 1865 to 3 per cent., and finally to $2\frac{3}{4}$ per cent.

* Dillon, *History of Irish Banking*.

The Provincial Bank of Ireland was formed in London, and commenced business in 1825; in consequence of its being established in London an office was opened there on 1st January, 1838.

The National Bank was founded in 1835, on a somewhat novel basis, *viz.*, having two distinct sets of shareholders, *viz.*, English and Irish. When a new branch was established the English shareholders contributed the same amount of capital as the Irish, and profits were equally divided. It was found, however, to be somewhat inconvenient; consequently, in 1837, the two stocks were consolidated, except at Clonmel and Carrick-on-Suir. These branches, however, in 1856, were amalgamated with the central establishment; in recent years this bank has opened several London branches.

The Hibernian Bank, established in 1825, was promoted by Roman Catholics, who were at one time excluded from the management of the Bank of Ireland; it endeavoured to issue bank notes, but this was opposed by the Bank of Ireland.

The Royal Bank of Ireland, established in 1836, took over the business of Sir Robert Shaw & Company, a private bank, dating from 1799; and although it endeavoured, like the Hibernian Bank, to issue notes, the Government refused to grant the privilege; some branches of this bank have been opened in Dublin.

As the north part of Ireland is noted for its commerce and manufactures, we naturally find that banking has flourished considerably.

There are three joint-stock banks established at Belfast, which are as follows: the Northern Bank, established in 1825, absorbed a private bank of the same name, and in 1888 opened a branch in Dublin, when the business of Messrs. Ball & Co. was acquired.

The Belfast Banking Company, established in 1827, was also originally a private institution.

The Ulster Bank, established in 1836, has been successful; in fact, similar to the other banks of a province which is distinguished for its enterprise, especially in shipbuilding and linen manufactures.

At Cork we have the last joint-stock bank established in Ireland, *viz.*, the Munster and Leinster Bank, formed in 1885 for the purpose of supplying the place of the Munster Bank which failed at that time.

Although a large number of private banks failed during the eighteenth century, probably due to the disturbed state of the country, the failures of joint-stock banks have not been so numerous, in fact, less than in the sister kingdom. The banks now in existence appear to be conducted on sound principles, and their business steadily increasing, although not so rapidly as in England; yet we could scarcely expect an agricultural country to accumulate capital so quickly as a manufacturing one.

The eleventh annual report of the Provincial Bank of Ireland for May, 1836, gives a good account of the progress of Irish banking:—

“To show the progress of competition it may be sufficient to state that prior to 1825, when the Act 6, George IV., c. 42, was passed, under which the Provincial Bank was established, the Bank of Ireland had no establishment out of Dublin; that in Dublin itself there were only four more—and these were private banks—and that in all Ireland there were no other than private banks, and those only in Belfast, Cork, Wexford and Mallow. From 1825 to 1834 banking offices in the chief cities and towns of Ireland had been gradually established by the Provincial Bank, the Northern Bank and the Belfast Bank, to the number of about fifty; while within the

short space of the last two years the offices of joint-stock banks having resident managers or agents, beyond fifty miles from Dublin, added to the branches of the Bank of Ireland, have increased to upwards of one hundred and twenty, and appear to be daily augmenting in number. Besides which there are a variety of stations attended on market-days by non-resident agents on behalf of one or other of such banks."

The following table will show the increase in the number of offices :—

1851 = 170 offices or 1 to every	38,300 inhabitants.
1872 = 365 " "	14,800 "
1875 = 404 " "	13,100 "
1878 = 409 " "	10,788 "
1883 = 542 (131 are sub-branches)	9,520 "
1901 = 690 offices or 1 to every	6,459 "

In 1902 nine new offices were opened, which shows the increase of banking facilities in the country.

It was impossible some years ago to state the amount of money lodged in all the Irish banks, because some of them did not publish any balance sheet; the following table shows the increase of the private balances in the Bank of Ireland, and the deposits of the Hibernian Bank, the National Bank, the Southern Bank, the Provincial Bank, the Royal Bank and the Ulster Bank (the figures for recent years comprise the whole number) :—

£
1840 = 5,567,000
1846 = 8,442,000
1852 = 10,773,000
1855 = 12,285,000
1860 = 15,609,000
1865 = 18,619,000
1870 = 24,366,000
1875 = 33,519,000
1880 = 29,746,000
1885 = 29,370,000
1903 = 50,438,000

All the banks now publish balance sheets, the amount of deposits being £50,438,000.

The year of formation, the paid-up capital, the number of proprietors and the number of offices of the Irish banks are as follows :—

	Formed.	Offices.	Capital.	1903 Dividends.
			£	
Bank of Ireland	1783	79	2,769,230	12
Northern Banking Company .	1825	53	500,000	12
Hibernian Bank	1825	69	500,000	5
Provincial Bank of Ireland .	1825	77	540,000	12
Belfast Banking Company .	1827	71	493,000	20
National Bank	1835	114	1,500,000	11
Ulster Bank	1836	66	500,000	20
Royal Bank of Ireland . .	1836	10	300,000	12
Munster and Leinster Bank, Ld.	1864	61	200,000	11½

The following table shows the present position of the Irish banks :—

LIABILITIES.

Deposits.	Notes.	Acceptances.	Total Liabilities.
£	£	£	£
50,438,000	6,786,000	269,700	£69,596,000

ASSETS

Banking Advances.	Stocks and other Securities.	Banking Premises.	Reserves.	Total Liabilities.
£	£	£	£	£
38,674,000	19,218,000	1,166,000	10,536,000	69,596,000

The present amount of deposits is £50,438,000, against assets comprising—cash £10,536,000, and investments £19,218,000.

The system of audit adopted by the National Bank ought to be mentioned, since it is in many respects unique. The shareholders appoint three of their number to inspect the books of the bank, and they can if necessary employ professional auditors to assist them in drawing up their statement; in this manner separate audits of accounts are brought before the shareholders at the annual meeting.

CHAPTER XII.

ACCUMULATION OF CAPITAL IN BANKS.

ONE of the most remarkable events in the commercial history of this country is the enormous increase of capital stored up in banks, principally for the purpose of extending our trade and commerce throughout the world. Such capital is also an indication of the accumulated wealth of this country ; and no one can deny the fact that our freedom of trade in the past has enabled us to build up a fund which is essentially necessary for maintaining our position as a great manufacturing country.

Various estimates have been given of the growth of deposits, and we shall briefly refer to the same :—

		Deposits.
1832-41	Mr. J. G. Hubbard . . .	£16,000,000 to £20,000,000
1847	Mr. Wilson . . .	200,000,000 to 250,000,000
		(Number of banks = 1,600)
1850	Mr. Newmarch . . .	260,000,000
1871	Mr. Palgrave . . .	662,000,000

Mr. Dun, in a paper read before the Statistical Society in 1876, gives the amount as £782,000,000, *viz.* :—

London Banks—		
Joint-stock		£93,400,000
Private		80,000,000
		<hr/> £173,400,000
London and Provincial Banks		60,400,000
Purely Provincial Banks—		
Private Banks }		
Joint-stock Banks }		
		256,000,000
		<hr/>
Total—England and Wales		£489,800,000

but in 1863 Post Office Savings Banks came into existence through the advocacy of the late Sir Charles Sykes of the Huddersfield Bank.

The following figures show the remarkable growth of these institutions :—

	Trustee Savings Banks.	Post Office Savings Banks.
	£	£
1820 . . .	2,915,000	
1841 . . .	24,474,968	
1851 . . .	28,931,000	
1860 . . .	41,258,000	
1870 . . .	37,959,000	15,099,000
1878 . . .	44,293,000	30,412,000
1901 . . .	51,966,000	140,392,000

This large sum of £192,000,000 gives some idea of the accumulation of national wealth.

Recently, in consequence of the amalgamation of various banks throughout the country, we are able to obtain a more accurate statement as to the amount of deposits held by the various banking institutions.

The following shows the position in 1903 :—

	Deposit and Current Accounts.
	£
England and Wales	645,100,000
Scotland	106,400,000
Ireland	50,400,000
Isle of Man	1,100,000
	<hr/>
	£803,000,000
Savings Banks	192,000,000
Colonial Joint-stock Banks with offices in London .	312,240,000
Foreign Joint-stock Banks with London offices .	217,663,000
	<hr/>
	£1,524,903,000

This great accumulation during recent years shows the rapid growth of capital in the United Kingdom.

Sir Robert Giffen in 1875 estimated the capital of the country to be £8,500,000,000 ; but the increase in recent

years must have been great, because in 1901 he thought the capital of the nation was not far short of £15,000,000,000, while the annual increase in ordinary times must at least be between £200,000,000 and £300,000,000. We can somewhat estimate the growth from Income Tax returns, which show a remarkable increase of £128,000,000 for a period of ten years ending in 1897.

CHAPTER XIII.

BANKING AND COMMERCIAL CRISES.

It is desirable to consider certain periods in the history of banking when, in consequence of commercial crises, there has been a withdrawal of deposits ; consequently the banks have been placed in a somewhat difficult position. The great foundation of our banking system is confidence, but when reckless speculation, on the part either of banks or of the commercial world, takes place, we get a feeling of distrust, and the result may be disastrous to the country.

The history of English commerce shows great fluctuations in prices of commodities, which are due to the laws of supply and demand. If any great catastrophe affects one industry, the effect is in time felt by others. This is partly due to the division of labour, which is the outcome of the expansion of trade. Manufacturers are able to produce goods in large quantities at a reduced cost in consequence of the division of labour ; this cheapening process increases the demand for commodities. On the other hand, we must not forget that the system has its disadvantages, because trades become more dependent upon one another. For example, we know how dependent the iron industry is upon coal ; the producer and consumer are therefore not brought into contact with each other, consequently when one fails a great number of intermediaries are affected.

We know that depressed agriculture causes stagnation

in trade, since it is still a large industry in this country. Banks in agricultural districts are considerably affected when that industry is suffering from depression.

If there is a series of bad harvests a less amount of capital is expended upon other trades, consequently during such periods we should expect to see the deposits in banks decrease.

Credit is singularly varying ; it confers advantages, but on the other hand there are corresponding disadvantages.

We have observed in a former chapter the disastrous effect upon banking by the indiscriminate circulation of bank notes, a form of credit which is now strictly regulated by Acts of Parliament.

Again, the use of credit enables capital to be transferred to places where it is more urgently needed ; as a rule we might say that capital finds its way to places where it can be utilised with better advantage. Credit also increases efficiency and facilitates the business of the country ; it tends to diminish the friction of exchange and to steady prices.

We have already noticed that production is stimulated by the use of capital ; another point to remember is, that in times of good credit bills issued against commercial transactions are taken readily, consequently years of improving credit are periods of rising prices ; and, *vice versâ*, when credit is bad we find that prices tend to fall.

There are great dangers attending our system of credit, and we shall notice that at various times the banks have not utilised the capital entrusted to them with care and discretion.

During commercial crises people exhaust their credit by converting floating capital into fixed. When prices rise, every one is anxious to secure large profits ; at such times the liabilities of speculators are increased quite out of pro-

portion to their means, consequently when called upon to meet their engagements they are unable to do so.

One of the drawbacks to our present system of credit is that it enables an unsound business to be carried on, so that when the crisis arrives the effect is great ; in fact, we lose in security what we gain in economy. The banks may exert a great power, and it must be their constant endeavour to keep aloof from the spirit of speculation ; by prudent management they are able to exercise great influence, and thereby prevent a sudden collapse of credit.

The system of large deposits in banks is peculiar to England, and this accumulation of capital affects trade and consequently prices. It has been stated by the late Mr. Bagehot that a rise in prices is caused by cheap money, cheap corn and improved credit ; when this occurs, the banks have a large number of applications for loans, so that the borrower may benefit by the rise. As a natural consequence the rate of interest rises, and generally at a rapid rate ; at such times the demand for capital is greater than the supply.

Whenever there exists a speculative period, the result is a system of overtrading ; liabilities are contracted which cannot always be met. At the same time we generally get an investing mania, brought about by the same causes. It has been truly stated in that excellent book, entitled *Lombard Street*, that any sudden event which creates a great demand for actual cash may cause a panic in a country where cash is economised and debts payable on demand are large. Accidental events, such as bad harvests, a failure of firms, etc., cause a sudden demand for cash, and may lead to a panic.

In fact, the characteristic of a true crisis is a previous destruction of wealth. Gold, notes and banks are, as it were, mere machinery required to carry on our modern

system of credit. At each successive crisis attention has been drawn to the system of banking, rather than to the fluctuation of trade or the speculative mania of the people.

We must not forget, however, that with the best system of banking it would be impossible for a bank to meet any large withdrawal of deposits. Ricardo says: "On extraordinary occasions a general panic may seize the country, when every one becomes desirous of possessing himself of the precious metals as the most convenient mode of realising or concealing his property. Against such panic banks have no security on any system."

The late Professor Jevons endeavoured to account for periodical crises by the appearance of spots on the sun's disc at intervals of 11.1 years. We know that the condition of trade is largely dependent upon the harvests not only at home but abroad.

It seems that the price of Delhi wheat reached a maximum in value every ten years. It is known that the amount of heat received from the sun is varying, and therefore we may suppose that the crops would vary in the same proportion. "The crops of Western Europe have always been strongly affected by communication with the Indies. Several of the crises are distinctly traceable to this cause, especially those at the beginning of the eighteenth century. That was a time of wild enterprise in the tropical regions, as the very names of the South Sea Company, the Mississippi Scheme, the Darien Project, etc., show. The Dutch, English and French East Indian Companies were then potent bodies, the constant subject of legislation and controversy. Thus it is my present belief that to the trade with India, China, and probably other parts of the tropical and sub-tropical regions, we must attribute the principal fluctuations in European commerce. Surely there is nothing absurd in such a theory when we remember that

the present crisis is at least partly due to the involvement of the City of Glasgow Bank in the India trade, through the medium of some of their chief debtors. Thus the crisis of 1878 is clearly connected with the recent famines in India and China, and these famines are confidently attributed to solar disturbance."

It would be interesting if we had Professor Jevons' opinion on the state of banking and commerce at a recent period, when there was an abundance of corn at very low prices concurrent with a certain stagnation in trade.

England is so dependent upon the harvests of the world that any great failure in the supply might have a disastrous effect upon credit.

A system of banking which is based upon lending money to unsound borrowers, thereby encouraging undue speculation, is not beneficial, but unfortunately many good banks suffer through a loss of credit brought about by the faults of other institutions. The cause of these disasters to banking and commerce is principally due to excessive speculation, which usually ends in a crisis or panic.

Whenever we get in this country a rapid accumulation of capital, it is usually accompanied by a great demand for investments, and this sometimes leads to speculative enterprises. For example, capital is expended say in making railways, digging mines, or constructing docks, which would not be reproduced for a long period of years. In order to carry out such enterprises, loans are contracted at banking institutions, and when the time for repayment arrives the borrowers are unable to meet their liabilities. If capital has been sunk in the manner already indicated, there is no great accumulation of it in banks, and the bankers' power to lend is naturally diminished. When merchants cannot obtain assistance, in order to

meet losses or calls on new undertakings, they begin to lose confidence in each other, and then we get the culminating point of a crisis, *viz.*, a panic, when suspicion rests upon every one. At such times depositors in banks may demand repayment of their capital, and thus banks are suddenly called upon to meet an additional strain upon their resources.

The system of deposits is not advantageous when there is a feeling of distrust in the money market, because at such periods the depositor is anxious to withdraw his capital, especially if he is not a customer. This was actually the case when the last Australian bank crisis took place; the depositors in this country were not concerned in the effect produced in Australia by the withdrawal of capital. The private bankers formerly would only accept deposits from their customers, because they considered that it was not their business to find investments for outsiders.

Modern banking, however, could not be carried on without deposits, but at the same time it is desirable to point out the risks involved in the business.

If bankers have lent money to persons for the purpose of speculation, they may possibly find themselves in possession of a large quantity of worthless securities which are unmarketable. On the other hand, if they have advanced money on good securities which are saleable, they stand a much better chance of surviving the crisis. At these critical periods the people refuse to see that gold, notes, banks, etc., are mere machinery, and that the crisis is quite distinct from such questions.

It will be important to notice the position and action of the Bank of England during commercial crises, because the returns of that institution give us a good record as to the course of events in the money market. The Bank has

been called upon at such times to exercise its great power in order to restore confidence and also to allay the panic which generally occurs. When a withdrawal of deposits from other banks has taken place, those of the Bank of England have generally increased, showing that at such times confidence in that institution remains unchanged.

We will now consider such crises in chronological order.

The first run upon bankers took place when the Dutch sailed up the Thames in 1667. The next crisis took place about twenty-five years later, and owed its origin to a large speculative undertaking, known as the South Sea Company, formed in 1711 for the purpose of trading in the South Seas, and was for a time a rival of the Bank of England. When we consider that the latter institution was in difficulties in the years 1704 and 1709, there is some reason for a comparison between the two companies.

The South Sea Company, by means of advertisements representing enormous advantages, managed to get the price of its stock raised from £290 on 7th April, 1721, to £890 on the 2nd June, but it fell rapidly and was quoted at £400 on 2nd September. Many of the goldsmiths and bankers had advanced money upon South Sea stock, and when the price of the stock rapidly fell, a run upon the banks occurred, so that many stopped payment, and some bankers absconded. There was also a run upon the Bank of England, but by means of a clever scheme it was stopped.

The success of the Pretender in Scotland in 1745 caused a disturbance of credit, when the notes of the Bank of England fell to 10 per cent. discount.

The year 1763 was remarkable as being the first of a series of commercial crises, caused by a too great expansion of credit. A large number of failures amongst the merchants of Hamburg affected those trading with that

place, and in order to stop the panic the Bank of England made advances to the extent of £1,000,000.

The commercial speculations of 1772 created another panic; this was exemplified by the number of bankruptcies, which amounted to 525. The failure of Messrs. Heale & Co., bankers in Threadneedle Street, intensified the crisis, and the Bank of England's aid was required in order to restore confidence.

After the close of the American War in 1782, a large expansion of our foreign trade occurred. Speculation became active, and this, combined with an injudicious issue of notes by the Bank, caused a drain of specie, which almost caused it to suspend cash payments. It is stated that the country bankers supported all kinds of wild projects by means of the issue of bank notes, and when called upon to pay them were unable to do so.

In the panic of 1793 no less than 100 out of a total number of 400 country banks stopped payment, and the remainder were in a critical condition. The commercial crises were attributed to the monopoly of the Bank of England, combined with its restricted issue of notes at times when a stringency of the money market existed. The fact of a previous destruction of wealth, combined with a depreciation in the value of commodities, was overlooked. No doubt the private bankers supported speculation by the issue of notes, but this was not of itself sufficient to cause the crisis.

The discussions on the currency, however, had a good effect, because the Bank Charter Act of 1844, which secured the convertibility of the note, was of distinct advantage to the country.

After the American War there was a period of prosperity throughout Europe; the usual course of events followed, *viz.*, an era of speculation. This was shown by the Bank

of England's note circulation, which rose from £6,000,000 in 1784 to £11,500,000 in 1792, but in the autumn of the latter year a series of failures occurred. On the 15th February, 1793, a house of considerable magnitude, deep in corn speculations, failed, and on the 19th the Bank of England refused to discount the bills of Lane, Son & Fraser, so that firm was obliged to suspend payment next day with liabilities of nearly £1,000,000. A great number of respectable firms were involved through this failure, and the panic soon affected the banks. The failures commenced at Newcastle, and although the partners in the banks at that place were opulent, yet their assets being locked up in securities which could not be realised, they were obliged to suspend payment. The banks at Exeter and in the West of England were almost the only institutions which survived the crisis.

These failures were attributed to the issue of bank notes without sufficient reserves.

A committee of the House of Commons recommended the issue of Exchequer Bills; this course was adopted by the Government, which had the effect of restoring confidence. When it was known that capital could be borrowed at a price then the alarm subsided.

The next banking crisis occurred in 1797, when some banks at Newcastle were in difficulties; the situation became so critical that an Act was passed allowing the Bank of England to suspend payment. It was thought that the laws affecting the Bank of England, and also of the currency, were the cause of financial troubles, but as Professor Jevons stated at a later period: "I must maintain, then, that under the present system the English currency is governed by the natural laws of supply and demand of a metallic currency, and not merely by artificial regulations. If the terms are interpreted aright we have

already a natural and free trade system of currency, and I venture to take this auspicious expression free trade from those who use it wrongly, and who confuse the free manufacture of currency with free trade in *capital*, the true business of the banker."

In 1807 the South American Continent asserted its independence, and speculation with that country was soon at its height. It is stated that clerks with about £100 capital were allowed by the banks to have discount accounts amounting from £5,000 to £10,000. By such means the bankers supported speculations, and credit naturally sustained a shock three years later, in 1810.

We have the following report of it: "The failures of houses of the highest respectability, both at London and at different provincial towns of Great Britain, have within the last month (August, 1810) been unprecedented in number and importance. A West India broker, who had been considered the first in his line, was, we are told, the prime cause of the stoppage of a banking house whose credit was previously unimpeached. The several banks in the country connected with the London house of course shared his fate, and from them the evil spread to merchants and manufacturers, traders, and, in short, to the very servants and dependants of these. . . . Speculation in Spanish wool, an article which has fallen about 50 per cent., was considered as the origin of the unlooked-for disaster."

Fourteen years later, *viz.*, in 1824, speculation was again active; the people had entirely forgotten their losses through lending so much capital to South America. A large number of companies were floated for constructing railroads, mines, canals, gas, etc., in number about 624, with a nominal capital of £372,000,000. This was followed

by a rapid rise of prices, but in a very short time there was a corresponding fall.

The bankers lent money to persons who speculated in all kinds of commodities, by means of the issue of bank notes, which, however, could not be paid on demand. Unbounded credit was followed by distrust, and a run upon the banks quickly followed. At this critical period the Bank of England very unwisely refused to discount any more bills, this intensified the crisis, which culminated in a panic.

On the 22nd November, 1825, Sir W. Elford's bank at Plymouth stopped payment; this was followed by Wentworth & Co., a great Yorkshire firm, the well-known house of Messrs. Pole & Co., besides three or four more London banks and sixty-three country banks. On the proposition of the Government, the Bank of England issued £1,000,000 of £1 notes, which fortunately happened to be in their possession, and also lent large sums by means of discounting bills; these measures afforded great relief to the merchants in London.

The Bank of England's note circulation rose from £19,000,000 (August, 1825) to £25,000,000 (February, 1826).

The bankers suffered immensely from want of confidence, and every possible scheme was adopted in order to stop the run.

A Cambridge bank advertised that it would afford facilities to the holders of its notes in order to exchange them for gold or notes of the Bank of England.

An Oxford institution exhibited so much gold on its counter that every one was satisfied as to its position, and a bank at Norwich stopped the run by displaying large quantities of Bank of England notes upon its counter.

The following tables will show the fluctuations in prices and the effect of the crisis on the Bank of England :—

SHARES IN 1824.

		Dec. 10, 1824.	Jan. 11, 1825.
	£		
Anglo-Mexican . . .	10 paid	33 pm	158 pm
Brazilian . . .	10 „	10 dis	70
Columbian . . .	10 „	19 pm	82
Real del Monti . . .	70 „	£530	£1,350
United Mexican . . .	10 „	£35	£155

	July to Nov., 1824.	Dec., 1824, to June, 1825.	Jan. to June, 1826.
Cotton, per lb. . . .	7½d. to 9d.	1/4 to 1/6½	6½d. to 7½d.
Indigo	10/4 to 12/10	21/- to 24/-	13/6 to 15/6
Spices (Cinnamon) . .	6/9 to 7/-	11/6 to 12/-	6/- to 6/9
Tobacco	2/- to 7/-	3/- to 9/-	3/- to 8/6
Silk	16/6 to 23/-	18/- to 29/10	13/3 to 16/-
Sugar	29/11¾	41/5	28/7½
Coffee	58/- to 60/-	76/- to 79/-	47/- to 49/-
Saltpetre	19/- to 20/-	34/- to 36/-	22/- to 24/-
Iron	£6 to £7	£11 to £12	£8 to £9
Lead	£23	£30	£22

SYNOPSIS OF CRISIS OF 1824.

Date.	Notes under £5.	Notes of £5 and Bank Post Bills.	Total Circulation.	Bills Dis- counted.	Bullion.
	£	£	£	£	£
1822, 31st Aug.	855,330	16,609,000	17,464,000	3,388,000	10,100,000
1823, 28th Feb.	681,500	17,716,000	18,392,000	4,107,000	10,400,000
„ 30th Aug.	548,500	18,683,000	19,231,000	2,801,000	12,600,000
1824, 28th Feb.	486,130	19,251,000	19,736,000	2,227,000	13,800,000
„ 31st Aug.	443,140	19,689,000	20,132,000	2,449,000	11,700,000
1825, 28th Feb.	416,730	20,337,000	20,754,000	2,466,000	8,700,000
„ 31st Aug.	396,340	19,002,000	19,398,000	5,486,000	3,600,000
1826, 28th Feb.	1,375,250	24,092,000	25,467,000	9,597,000	2,400,000
„ 31st Aug.	1,161,000	20,402,000	21,500,000	2,950,000	6,700,000

The country soon recovered from the effects of this crisis, but scarcely ten years had elapsed before the mania for speculation was again rife.

There were a large number of joint-stock companies constituted for the following projects, *viz.*: banks, railways, canals, gas, mining, insurance, etc.; during the years 1836-37 no less than 300 to 400 companies were formed.

In America there was a great deal of speculation, which led to the failure of 250 houses in 1837.

The Bank of England was censured for its conduct during this crisis; it refused to discount all bills bearing the endorsements of joint-stock banks, and requested the Liverpool branch not to discount any bills for merchants dealing with the United States. This withdrawal of financial support intensified the panic. The bullion in the Bank rapidly decreased:—

		£
January, 1834 . . .	Circulation . . .	18,000,000
	Bullion . . .	9,500,000
„ 1836 . . .	Circulation . . .	18,000,000
	Bullion . . .	4,500,000

SYNOPSIS OF CRISIS OF 1837.

Date.	Circulation.	Bullion.	Bills Discounted.
	£	£	£
1834, 25th February . .	19,050,000	9,225,000	1,800,000
„ 26th August . .	19,195,000	7,303,000	2,500,000
1835, 24th February . .	18,510,000	6,289,000	2,100,000
„ 25th August . .	18,085,000	6,255,000	2,600,000
1836, 20th February . .	18,181,000	7,787,000	2,900,000
„ 30th August . .	18,018,000	5,250,000	4,400,000
1837, 28th February . .	18,165,000	4,077,000	11,200,000
„ 29th August . .	18,827,000	6,548,000	5,100,000
1838, 27th February . .	18,925,000	10,471,000	3,200,000
„ 28th August . .	19,488,000	9,540,000	2,900,000

This crisis was followed by another in 1839, which was due to a succession of bad harvests, the financial condition

of America, and lastly to the unsatisfactory condition of credit throughout Europe.

In September of that year the bullion in the Bank of England was reduced to £2,816,000, and that institution was obliged to borrow £2,000,000 from the Bank of France in order to strengthen its position. The rate of discount rose from $3\frac{1}{2}$ per cent. to 6 per cent. in October of the same year.

Prior to the passing of the Bank Act of 1844, it was the custom of the Bank to keep one-third of its liabilities in gold. When the Act was passed it was supposed that all these commercial disasters which had affected banker and trader alike would entirely disappear. Unfortunately, three years later it was discovered that panics, destruction of capital and high rates of interest would occur from time to time, just as was the case prior to the passing of the Act.

Some people believed that the laws regulating the issue of bank notes were the cause of those events which affected the trade of the country, and stated that if the note circulation was placed on a satisfactory basis, no more panics, etc., would occur. The real cause of such disasters was, unfortunately, not properly understood ; it has been already pointed out that many errors have arisen in consequence of questions relating to banking and currency being considered as one subject.

This was shown in the crisis of 1847, when Sir Robert Peel's Act was attacked on all sides ; no doubt the opposition was partly due to its promoters, since they stated that the Act would accomplish great things, and place the commercial transactions of the country on a satisfactory basis.

The crisis of 1847 was very similar to those which had previously occurred ; a great accumulation of capital created a want for new investments ; this increase was shown by

the large amount of bullion in the Bank of England, Government Stock being at par, and also by low rates of interest.

The following were the rates at that time :—

7th September, 1844, to 11th October, 1845 = $2\frac{1}{2}$ per cent. ; then 3 per cent., $3\frac{1}{2}$ per cent. back to 3 per cent., and finally rising to 4 per cent. on 23rd January, 1847.

Mr. Cotton, the Governor of the Bank of England, stated that the true cause of the crisis was the great number of investments in speculative enterprises, more than the capital of the country would permit, the proportion of fixed to floating capital being far too great.

These speculative enterprises were chiefly in railways, cotton and iron ; the failure of the potato crop in Ireland and a deficient harvest in this country required more capital, but owing to the previous lock up there was not any available.

The large imports of grain from abroad caused a sudden fall in prices, and led to the failure of many houses in Mark Lane. The Bank of England refused to lend money on stock or exchequer bills ; in fact, credit was very much shaken. The failure of many banks followed, which included the Royal Bank of Liverpool, the Liverpool Banking Co. and the Union Bank of Newcastle.

The London merchants asked the Government to suspend the Bank Act, and, when this was agreed upon, the mere announcement had the desired effect of restoring confidence, although no infringement of the Act really occurred. It seems to be the best policy for the Bank of England to lend freely during times of commercial crisis, because if people know that loans can be obtained at a price, they are not so eager to get accommodation, and by such means a crisis may not ultimately develop into a panic.

The Bank of England raised its rate from 5 per cent. to $5\frac{1}{2}$ per cent., and finally to 8 per cent. The discounts of that institution increased to an enormous extent:—

	£
Discounts—1844	2,000,000
2nd October, 1847	10,000,000
9th „ 1847	11,000,000
23rd „ 1847	12,500,000

The reserve was reduced from £3,409,000, 2nd October, 1847, to £1,176,000, 30th October, 1847.

SYNOPSIS OF CRISIS OF 1847.

Date.	Circulation.	Bullion.	Reserve.	Bills Dis- counted.	Rate.	Amount of Exports.
	£	£	£	£		£
1841, 27th Feb. .	16,411,000	4,400,000	...	...	5	...
„ 31st Aug. .	17,530,000	4,800,000	...	...	5	51,500,000
1842, 28th Feb. .	17,013,000	6,300,000	...	...	4	47,300,000
„ 31st Aug. .	20,071,000	9,800,000	...	...	5	...
1843, 28th Feb. .	20,284,000	11,100,000	...	...	4	52,200,000
„ 31st Aug. .	19,939,000	12,300,000	...	...	4	53,500,000
1844, 29th Feb. .	21,148,000	16,200,000	...	...	4	...
„ 31st Aug. .	20,480,000	15,315,000	7,732,000	2,141,000	$2\frac{1}{2}$	60,100,000
1845, 28th Feb. .	19,802,000	15,253,000	8,889,000	2,422,000	$2\frac{1}{2}$	...
„ 30th Aug. .	21,059,000	15,592,000	7,959,000	4,445,000	$3\frac{1}{2}$	57,700,000
1846, 28th Feb. .	20,921,000	13,776,000	6,691,000	13,137,000	3	...
„ 29th Aug. .	20,426,000	16,366,000	9,450,000	6,067,000	4	58,800,000
1847, 27th Feb. .	19,330,000	12,045,000	6,017,000	8,879,000	$5\frac{1}{2}$	...
„ 28th Aug. .	18,236,000	9,146,000	4,330,000	9,163,000	5	...
„ 2nd Oct. .	18,712,000	8,565,000	3,409,000	10,399,000	5	...
„ 9th „ .	18,640,000	8,409,000	3,322,000	10,978,000	$5\frac{1}{2}$	...
„ 15th „ .	19,360,000	8,431,000	2,630,000	11,907,000	...	...
„ 23rd „ .	20,318,000	8,313,000	1,547,000	12,492,000	8	...

PRICES OF RAILWAY IRON.

	£	s.	d.	
1843	6	9	4	per ton.
1844	6	14	3	„
1845	10	15	10	„
1846	10	6	8	„
1848	6	2	10	„

Consols fell to 85.

The next crisis occurred in 1857; this was principally due to merchants who had speculated far beyond their

capital by means of fictitious credit. Money was obtained from the bankers by means of accommodation bills, or bills supposed to be drawn against value received.

There was also a great deal of speculation in America; the failure of many houses in that country directly affected those banks in the United Kingdom which held American bills. No less than 150 banking houses in America failed, and this was the cause of many banks suspending payment in this country. The Boro' Bank of Liverpool, the Western Bank of Scotland, the City of Glasgow Bank, Sanderson & Co. and Dennistoun & Co. closed their doors.

The directors of the Bank of England appealed to the Government for a suspension of the Bank Act. When this was done, on 12th November, 1857, the mere announcement had a good effect, because it was the means of restoring confidence. Although the Act was suspended, the notes issued in excess, without any reserve of bullion, only amounted to £800,000. This shows that the suspension of the Act was not in itself of any value, but it was the means of allaying the wild alarm which existed in the country. The loans advanced by the Bank of England on private securities increased from £20,404,000 to £31,350,000. A high rate of interest was charged, to prevent those who really did not require advances from obtaining loans. The reserve of the Bank was reduced from £4,606,000, 3rd October, 1857, to £957,000, 14th November, 1857.

PRICES IN 1857.

	July, 1857.	January, 1858.
Bengal Silk	15s. to 33s. 6d.	11s. to 24s.
Tallow	80s.	60s.
Sugar	55s.	35s.
Cotton	7d.	6d.
Tea	1s. 3d.	1s.

Taken generally, a fall of 20 to 30 per cent.

SYNOPSIS OF CRISIS OF 1857.

Date.	Circulation.	Bullion.	Reserve Notes and Coin.	Bills Discounted.	Rate.	Deposits in Chief Banks.	British Exports.
	£	£	£	£		£	£
1850, 23rd Feb.	18,902,000	17,120,000	12,233,000	2,388,000	2½	11,900,000	71,400,000
" 31st Aug.	19,962,000	16,770,000	11,086,000	2,603,000	4	...	...
1851, 22nd Feb.	18,713,000	14,436,000	9,722,000	4,115,000	3	14,700,000	74,400,000
" 30th Aug.	19,716,000	14,362,000	8,645,000	5,393,000	2	...	...
1852, 28th Feb.	20,523,000	19,239,000	12,714,000	3,245,000	2	17,400,000	78,000,000
" 28th Aug.	27,620,000	21,914,000	13,292,000	2,716,000	3	...	...
1853, 26th Feb.	21,990,000	18,191,000	10,200,000	5,845,000	3½	21,300,000	99,000,000
" 27th Aug.	22,776,000	16,963,000	8,186,000	5,457,000	5	...	...
1854, 25th Feb.	21,690,000	16,286,000	8,386,000	5,049,000	5	25,600,000	97,200,000
" 26th Aug.	20,018,000	13,635,000	7,587,000	6,319,000	5	...	...
1855, 24th Feb.	19,062,000	13,045,000	7,982,000	6,066,000	3½	28,300,000	95,700,000
" 25th Aug.	20,042,000	15,546,000	9,503,000	5,751,000	4	...	...
1856, 23rd Feb.	18,541,000	10,575,000	6,509,000	8,883,000	4½	33,000,000	115,000,000
" 30th Aug.	20,124,000	12,387,000	6,736,000	4,446,000	6	...	...
1857, 28th Feb.	18,597,000	10,344,000	6,222,000	8,559,000	5½	37,700,000	122,000,000
" 29th Aug.	19,324,000	11,501,000	6,650,000	7,893,000	8	...	...
" 24th Oct.	19,766,000	9,370,000	4,077,000	9,036,000	8	...	...
" 31st "	20,372,000	8,732,000	2,804,000	11,105,000	8	...	...
" 4th Nov.	20,267,000	8,498,000	2,705,000	11,439,000	10	...	...
" 11th "	20,183,000	7,171,000	1,461,000	13,233,000	...	...	...
" 18th "	21,406,000	6,484,000	1,552,000	16,103,000	...	...	...
" 25th "	21,340,000	7,264,000	2,397,000	17,376,000	...	...	...
" 2nd Dec.	21,102,000	7,356,000	2,728,000	17,788,000	...	...	...

The *Economist* gives the following account of the securities which were circulating in the market :—

" Such securities were a pure speculation on the future, and a speculation subject to one principal and many smaller casualties.

" Take the case of a railway ; the line must be finished and placed in actual working before the obligations repre-

senting its cost can have any ascertained value at all. An unfinished railway or dock has no value whatever. In the second place, the line must not only be finished and actually worked, but in order to impart value to the bonds and shares there must be a positive profit surplus. The difference between securities such as these, wholly dependent upon future and uncertain events to happen at distant and irregular dates, and liable to become worthless by the premature stoppage of the undertaking, and the class of securities which long experience has shown to be best suited to the requirements of the bankers and money dealers, is not marked in its character, but so wide and glaring as to prepare any prudent person to expect mischief."

After this crisis trade revived, and a large number of finance companies came into existence for the purpose of securing all kinds of imaginary profits. From 1858 to 1868, 300 companies were formed, with a nominal capital of £504,000,000, and during this period the year 1866 alone witnessed the formation of seventy-five companies, with a capital of £61,000,000.

Companies in 1866.							Capital.
							£
17 Banks	.	.	.	.	.	.	25,000,000
25 Finance	.	.	.	.	.	.	9,000,000
9 Insurance	.	.	.	.	.	.	7,000,000
24 Shipping	.	.	.	.	.	.	20,000,000

The new banks transacted all kinds of business with foreign countries, and their success depended largely upon the state of trade with such nations. The finance companies advanced capital upon all possible undertakings, through the medium of bills kept in circulation.

The crisis of 1866 was started by the failure of Messrs. Overend, Gurney & Co. : this house, which had then

been recently converted into a company, was in its earlier days eminently successful. It is stated that in the year 1860 the partners divided £190,000 as profit; its position in the money market was supposed to be of the highest character, so that the announcement of the failure had a disastrous effect. Lombard Street was impassable, and it was stated that no such panic had taken place since 1825.

Overend, Gurney & Co. had lent money to support all kinds of speculative enterprises, including the building of ships for the increased trade of the country.

The following account gives a graphic description of the great excitement caused by the stoppage: At mid-day the panic was at its height; the demand for accommodation at the Bank of England was very great, so that its reserve fell to £730,000, although three weeks earlier it had stood at £5,844,000. Its loans on private securities increased from £18,507,000 to £33,447,000; the rate of interest rose to 10 per cent., remaining at that figure for eighty-eight days.

The directors asked the Government to suspend the Bank Act; this was granted, and its announcement had the same effect as in former years. Confidence was restored, but no infringement of the statute really took place.

The following table will show the Bank rate in panic years:—

1797 to 1837, Bank rate 5 to 4 per cent.			
1839	„	6	per cent.
1847, 2nd Oct.	„	5½	„
„ 23rd Oct.	„	8	„
„ 24th Nov.	„	7	„
1857, 3rd Oct.	„	5½	„
„ 24th Oct.	„	8	„
„ 20th Nov.	„	7	„
1859	„	2½	„
1860	„	5	„
1861	„	6	„

} panic year.

1862 to 1863	„	3 to 4 per cent.	
End of 1863	„	8 per cent.	
1864, Sept.	„	9 „	} panic year.
1866, 25th April	„	6 „	
„ 2nd May	„	7 „	
„ 9th May	„	9 „	
„ 16th May	„	10 „	

The effect of the panic of 1866 was so great that Lord Clarendon issued a despatch to foreign states, informing them that although the country had sustained serious losses, yet its trade was still *bonâ fide*.

The banks that failed in 1866, besides Overend, Gurney & Co., were the following :—

Barned's Bank, Liverpool.
 English Joint-Stock Bank.
 Oriental Commercial Bank.
 New Zealand Banking Co.
 Hallett, Ommaney & Co.
 Imperial Mercantile Credit.
 Commercial Bank of India.
 European Bank.
 Robinson, Coryton & Co.
 Alliance Financial.
 Bank of London.
 Consolidated.
 Agra & Masterman.

Price of Bank Shares.	1865.	Jan. 1, 1866.	May 12, 1866.
Agra & Masterman . . .	86 pm	33 pm	1 dis
Alliance	10½	4½	10
Barned . . . . .	...	...	...
Bank of London	22	13 pm	15
City	15	12	5½ pm
Commercial of India . .	7	5	no price
Hindustan	6	8	16 dis
London and County . .	63	59	47½ pm
Joint-Stock	41	36	27
London and Westminster	80	77	70
Union of London . . .	30	39	32

SYNOPSIS OF CRISIS OF 1866.

Date.	Circulation.	Bullion.	Reserve.	Bills Discounted.	Rate.	Deposits in Banks.	Exports.
	£	£	£	£		£	
1863, Feb. 25	19,117,000	14,614,000	9,253,000	7,066,000	4	54,000,000	144,600,000
„ Aug. 26	20,993,000	15,319,000	8,141,000	6,716,000	4	...	...
1864, Feb. 24	19,675,000	13,819,000	8,028,000	7,807,000	7	67,000,000	160,400,000
„ Aug. 31	20,738,000	12,980,000	6,142,000	9,141,000	8	...	...
1865, Feb. 22	19,659,000	14,600,000	8,254,000	7,950,000	5	67,000,000	165,800,000
„ Aug. 30	21,598,000	14,490,000	6,618,000	9,818,000	4	...	...
1866, Feb. 28	20,768,000	13,967,000	7,345,000	7,253,000	7	69,000,000	188,900,000
„ May 2	22,873,000	13,509,000	4,839,000	8,834,000	6	...	...
„ „ 9	22,345,000	13,156,000	4,950,000	9,249,000	7·8	...	...
„ „ 16	26,121,000	12,324,000	731,000	13,831,000	9·10	...	...
„ „ 23	25,469,000	11,858,000	831,000	14,501,000	10	...	...
„ „ 30	26,019,000	11,879,000	415,000	16,512,000	...	...	...
„ June 6	25,453,000	13,279,000	2,167,000	16,003,000	...	...	...

The bank failures since that time have been comparatively few, although in 1875 several institutions lost considerably through discounting accommodation bills.

The following is a list of failures of private, joint-stock and foreign banks in recent years :—

1873 = 5
 1874 = 5
 1875 = 3
 1876 = 2
 1877 = ...
 1878 = 8
 1885 = 1

The large number in 1878 included the City of Glasgow Bank, mentioned under Scotch banking, and the West of England and South Wales District Bank; both of these institutions had lent to individual customers large sums of money, quite out of proportion to their capital.

The West of England Bank had advanced to one firm nearly £500,000, although its capital was only £750,000. This money was locked up in the worst kind of investment, *viz.*, collieries, mines and iron works. When the directors endeavoured to obtain repayment of capital ad-

vanced upon these undertakings, they were unable to do so. If they had adopted the regulations imposed by law on the State Banks of the United States, which enacts that no bank shall advance to any one person an amount exceeding one-tenth of its capital, then it would have been impossible for this bank to have failed with such heavy liabilities.

A similar course of events occurred in 1890, when large sums of money were advanced to Argentina, and created a crisis which fortunately was averted by the action of the Bank of England. As this year is worthy of special notice, further reference will be made to it when considering the money market.

Many practical lessons can be learnt by studying these commercial disasters. The failures of many banks might be traced to the fact that, in order to pay large dividends, great risks have been undertaken, the ultimate effect being disastrous to banking and commerce. Merchants cannot obtain capital for speculative purposes unless the banks provide the same to some extent. In times of prosperity credit is abused, and by such means the trader incurs liabilities which he is unable to meet; this leads to a crisis, and then it is discovered that capital, not income, has been spent. Capital is sunk on all kinds of undertakings, which cannot be reproduced for many years; advances are made upon mills, railways, docks, mines and machinery, instead of bills representing trade transactions.

Again, capital is advanced upon stocks and shares, which sometimes gives a fictitious value to those securities. When a sudden fall in prices takes place, a bank is liable to incur losses on such depreciated securities. The cry is raised during crises for more notes, but the trader does

not want credit documents, but a sum of money placed to his credit, against which he can draw cheques.

Banking must always be conducted with prudence and caution, not only to progress, but also to benefit the community. A bank may be called upon at any moment to repay its deposits; therefore it is necessary to be always prepared for such a contingency.

Again, as fluctuations in value are one of the features of a crisis, it is always desirable to have a good margin on securities deposited as cover.

Loans should only be granted for short periods, as it is well known that even a week may sometimes show great changes in trade and credit.

Another important point is to distinguish between a marketable and an unmarketable security; we know that Consols as an investment is good, because the stock can be sold at a moment's notice, even in times of commercial crises. For example, large blocks were sold during a recent crisis without affecting the price to any great extent. There are many securities which can easily be sold, whilst for others the market is so limited that they cannot be realised for a considerable time.

Securities which are not quoted on the London or Provincial Stock Exchanges should not be accepted as security. The marketability of a security is therefore an important one, and for this reason loans secured against dock warrants, say of tea, coffee or sugar, would be in many ways preferable to those on deeds or mortgages of land.

CHAPTER XIV.

BANKING PROFITS.

THE RATE OF DISCOUNT.

IF a stranger to the great Metropolis visited the Bank of England on a certain day in the week, *viz.*, Thursday, he would witness a sight which might somewhat puzzle him. He might observe in one of the corridors a crowd of persons, composed of telegraphic messengers, officials from various banks, discount houses and other kindred institutions, waiting patiently until a notice is displayed on the wall, stating that the rate of discount is so much per cent., or that no alteration has been made. Immediately this announcement takes place, the crowd quickly disappears. All this excitement would naturally puzzle a stranger, and he might ask a series of questions such as—What is the meaning of the term discount? Why should the Bank of England fix the rate? And again, What causes the rate to fluctuate?

We shall endeavour to answer some of these questions, which are of great importance to the mercantile world. These changes in the bank rate of discount are especially important to the banks of this country, since their profits or dividends are largely dependent upon the rate of interest. At every bank meeting reference is made by the chairman to the rate of interest ruling in the money market during the preceding six months, and what effect

such rate has had upon the profits of that particular bank. The causes and effects of such changes are rather of a complex character, because every year the English money market has to take note of new developments of trade and commerce.

As Professor Marshall justly stated at a meeting of the British Association : “ When economic problems become more complex every year, the necessity of studying them from many different points of view, and in many different connections, becomes more urgent ”.

The Bank of England being, we might say, the most important storehouse of capital, has assumed the responsibility of fixing the price for the loan of capital. The variations in the amount of loanable capital existing in this country cause the price to fluctuate.

There are various forms of capital, but there is only one which concerns us—and that is floating or circulating capital. This kind of capital has been defined by J. S. Mill as that “ which fulfils the whole of its office in the production in which it is engaged by a single use ”. Other kinds, such as houses, land, machinery, etc., it will not be necessary to consider, although the income derived from such property would increase the amount to be utilised as loans by those who can profit by its employment. Capital is said to be the result of saving, or a sacrifice of present enjoyment for the sake of the future.

The income derived from the loan of capital is called interest, but we find the term discount used at the Bank of England. This word, however, in reality means the same, because discount is the difference between a sum of money due at a future period and its present value, or a deduction that is made from the amount of a debt that is paid before it is due. The amount deducted depends upon the value of money, or what we term interest.

There are other large houses grouped around the Bank of England, and they collectively are known as the organised market for the loan of capital, or, in other words, the money market. When we are standing inside the Bank of England we are, as it were, in the centre of the market.

The value of capital, like every other commodity, is mainly dependent upon the laws of supply and demand, but it differs from other commodities in being liable to great fluctuations, which are caused by other influences, such as the state of credit and the annual supply of gold received from the mines. It is somewhat difficult to see the effect upon the rate of interest, but the amount of cash held as reserve or for small change are two important factors. For example, when wages and prices are rising, more cash is required, and this can only be obtained from banks who draw upon their reserves at the Bank of England. This institution is, as it were, the pivot upon which depends the value of capital, especially in the short loan market. The price, however, for the loan of capital depends upon the state of the market, in the same manner as the price of iron, tea or coal is regulated.

In the money market, however, we do not ask the price of capital, but the rate of interest; thus price and interest with regard to capital would be synonymous.

We will endeavour to state briefly some of the causes which affect the supply of capital. It has been already stated that accumulations are dependent upon self-denial. The people forego pleasures for the sake of future enjoyments; an increase of *surplus* income above the necessities of life augments the *power* to save, and an increased regard for the future increases the *will* to save. Capital is originated by these means; and then we have people who, having become possessed of it, and not re-

quiring the same for their own use, are so eager to lend to others that they will accept a constantly lower and lower rate of interest. Thus we have fluctuations of interest, caused by an eagerness to lend.

Again, the accumulations of capital are dependent upon the rate of interest; if the rate is high, people save in order to obtain the advantage of a larger return for their capital; but, on the other hand, if low, the return is too small for the effort required to attain that object.

The following formula shows how rapidly capital accumulates at compound interest. Thus if I = rate of interest, then $\frac{69}{I}$ = the number of years for a sum of money to double itself. Thus if $I=5$, then a sum of money would double itself in 13·8 years.

At the present time the growth of capital does not show any sign of overtaking the growth of the scope for its employment, although the recent war in South Africa has been the means of absorbing a large amount, the effect being to create a demand for some considerable time. It however happens that at stated periods there is a vast accumulation of capital, but in consequence of previous losses there is a want of confidence, and consequently a dearth of new undertakings.

“ In the market the rate of interest cannot fall beyond that limit at which it only offers just sufficient inducement to those who are on the margin of doubt whether to save or not. For if it did, there would be a gradual shrinkage of capital relatively to the growing demand for it. Its marginal utility would rise in consequence of this relative scarcity, and therefore the rate of interest which is paid as the price of loans would rise also.” *

With regard to the demand for capital we find it is

* Marshall's *Economics of Industry*.

largely dependent upon the population, the natural resources of the country and the state of trade. Thus the demand would vary with the prosperity of the country.

The commercial business transactions of this country are effected by means of borrowed capital. The trader enters one of the storehouses of capital designated a bank, and borrows capital, for which he pays a certain rate of interest. With such resources he is able to purchase goods, and sell again at a profit, after paying interest to the bank for the loan of the same. The trader's net profit would be the difference between the amount as interest paid to the banker and that charged to the purchaser of his goods.

One of the reasons why the trade of this country has progressed so rapidly is due to the fact that capital can be borrowed at a low rate of interest. We have given some elementary principles with regard to the laws of supply and demand in connection with capital, and have also stated that, unlike other commodities, it is subject to great fluctuations. Although we shall consider these fluctuations, yet it will be convenient to mention at this point why capital is subject to great changes. The great force at work which causes such effects is the state of credit. The greater portion of the capital of the country finds its way into the banks, because the depositors trust such institutions with their surplus funds, and borrowers must be found who require the loan of capital, or else it would lie idle and no profit made: this is especially the case when interest is allowed on money deposited. The banks, therefore, act in the capacity of brokers: on the one hand they take capital from the depositors and lend it to others, *viz.*, the borrowers. We can easily understand that if at any time public confidence in such institutions becomes shaken, deposits may be withdrawn at short notice. Banks are, therefore, obliged to protect themselves from sudden

withdrawals by retaining a portion of their assets, called the reserve fund, in order to meet such contingencies. The tendency of the present day is to utilise surplus funds as much as possible in order to avoid any waste ; that is to say, to prevent capital from lying idle. This is, of course, beneficial in one way, because it increases the profits, but, on the other hand, it makes our banking system a very delicate one. For example, during a speculative period there would be no capital available to meet a sudden demand. At such times traders exhaust their credit by borrowing in excess of their capabilities to repay, and thus assume greater liabilities which can only be met by additional assistance from banks. We should expect, therefore, to see great fluctuations in the rate of interest when a speculative mania exists, because of a dearth of capital, created in some degree by the small reserves held in consequence of a great increase in loans.

The state of credit is therefore of great importance in relation to capital. We have seen that a vast system of credit is founded upon the reserves of the banks, which are the great storehouses of capital, and consequently any increase or decrease in the proportion of such reserves must have a great influence upon the rate of interest.

The following remarks of Mr. Wynnard Hooper, at a British Association meeting upon the London Money Market, state clearly the present position of capital. He says :—

“ The volume of business is larger, and the liabilities of London and the whole country are much larger, but the reserve held against them is only slightly larger than was the case twenty years ago. The deposits of banks have enormously increased. Those of the fourteen principal London banks have risen from £103,000,000 in 1870 to £178,000,000 in 1889. Other banks’ deposits have also

increased, and a larger proportion of the deposits are kept in London to be lent. On the other hand, the reserve of the Bank of England is, on the average, very little larger than it was during 1870-79. Of course, the reserve is now more efficient than it used to be, for reasons already given, but nevertheless it is too small."

The deposits of ten London banks are now £230,000,000.

CHAPTER XV.

BANK OF ENGLAND RATE.

THERE were many reasons why the Bank of England became the great central organisation for determining the value of money or capital in the market. It has already been noticed that the Bank possessed the exclusive right of joint-stock banking until the year 1826, and in addition to this monopoly, its large capital gave it a position above any other institution as a lender of money.

Besides its capital, the Bank had the privilege of issuing notes, which, of course, meant additional resources. In the year 1718 the note issue was £1,829,930, and has rapidly increased, the present circulation being about £52,000,000. Thus, from two sources, *viz.*, subscribed capital and note issue, the Bank of England was a formidable opponent to the banking community. We can therefore understand how this institution with large resources became great in finance and assumed the responsibility of fixing the rate, or the price for the loan of capital.

Another important fact must not be forgotten, and that is the connection between the Bank and the State. It was the custodian of Government Deposits, and thus had large resources at its command. Again, when the Government required assistance, the Bank of England made advances or floated various loans in the market; in fact, our National Debt came into existence through its aid, and thus from an early period the Bank and the Government have been allied.

In return for services rendered to the State, the Bank naturally looked to the Government for assistance during commercial crises and panics. The privileges bestowed upon it were as follows: The use of the Government balances, which at times are very large (the amount at present varies from £7,000,000 to £15,000,000). The community naturally thought that if the Government could trust the Bank, their savings would be quite secure. Again, it had, as already stated, the monopoly of joint-stock banking until the year 1826, and consequently held large deposits before other joint-stock banks came into existence; finally, it was the only joint-stock bank in London which could issue notes; thus from many singular events the Bank became the holder of the cash reserve.

There is rather a curious illustration showing the connection between the Bank and the Government. In the year 1797 Mr. Pitt, as Chancellor of the Exchequer, was afraid there would not be enough specie in the Bank to meet foreign payments, and compelled it not to pay gold for notes issued. Naturally a bank which had this great privilege must obviously assume a commanding position—in fact, an institution with a charmed existence. There are, however, two important incidents which materially assisted towards making it the principal dealer in capital, and in such capacity to state the price for loans.

The first was in consequence of the London banks opening accounts at the Bank of England, since they found it convenient to keep their reserves with an institution which had vaults somewhat better protected, and, as the Bank issued notes, it was found desirable to retain them rather than gold; especially as the former were a legal tender for payment of debts, liabilities could be discharged, thus avoiding the use of coin to some extent.

The balances of the London banks are large; from the

Government returns the amount in 1844 was £1,000,000, and increased to £7,500,000 in 1872. Since that date no particulars have been given as to the present amount.

In 1853 these balances never exceeded the reserve by 20 per cent., but the proportion increased to 60 per cent. during the period 1864-72.

	Proportion of Reserve to Liabilities.	Proportion per cent. Bankers' Balances to Reserve.
Thus—1846-54 .	51 per cent.	22 per cent.
1855-63 .	43 „	48 „
1864-72 .	42 „	63 „

During the panic years of 1847, 1857 and 1866 the reserve of the Bank of England was insufficient to meet the bankers' balances.

	£
Thus—1857, Bank's Reserve	1,462,153
London Bankers' Balances	4,649,600
1866, Bank's Reserve	1,202,810
London Bankers' Balances	7,930,000

This additional capital which the Bank obtained from the London banks considerably augmented its resources, and any sudden withdrawal of such balances must react upon the rate of discount, since fluctuations in the rate are dependent upon the reserve of notes and gold.

The second incident was that it became the lender of capital to outsiders, *viz.*, to those who did not keep a banking account, which is quite different from the practice of other banking institutions.

The applications for loans at the Bank of England have been large during periods of panics and commercial crises, and the statistics given for the years 1847, 1857 and 1866 show to what extent the community required assistance. Thus, at various times the Bank of England has lent considerably, and assumed a responsibility over the money market by thus giving financial assistance to outsiders. At such periods all who held good securities received

accommodation ; the importance of this policy cannot be overrated, because, as we have already noticed, English trade is conducted partly by means of borrowed capital, so that if the trader could not discount bills he would soon be obliged to suspend payment.

The merchant purchases goods and pays for the same by means of bills drawn upon him, say three months hence, being enabled to meet such bills by discounting others received for goods sold. It is therefore of vital importance that at all times he is able to obtain accommodation when required. The Bank of England has, therefore, been of immense service to the commercial community at periods when capital is scarce, or a feeling of distrust has pervaded the mercantile world. Its good management is therefore of the highest importance ; when the deposits of other banks have diminished, in consequence of a want of confidence on the part of the depositors, the deposits of the Bank of England have invariably increased.

The last incident in its history is with regard to the note circulation, but the action of the Bank is purely mechanical ; in fact, as the late Mr. Bagehot stated, the office could be removed to Somerset House.

The Bank is allowed to issue £18,450,000 of notes against securities, but for any amount issued in excess the Bank must hold gold and silver in reserve. A limit was fixed by the Act of 1844, in order to secure the convertibility of the note.

The profit derived by the Bank from such issue is derived from interest-bearing securities ; the Government, however, receives a moiety, which is about £175,000.

The money market is somewhat affected if gold is taken from the Bank of England ; when the causes of fluctuations in the rate of interest are considered it will

be seen that gold withdrawals are of some importance. If the Issue Department was, however, removed to Somerset House, as already stated, it would be interesting to know whether the loss of, say, a million of gold would affect market rates to the same extent as under the present conditions.

The weekly reports of the banking department are, nevertheless, of great importance to the outside market, and are keenly scrutinised in order to ascertain what are the economic conditions which possibly might affect the value of money within a short space of time.

We see in the daily papers an analysis in the following form :—

BANKING DEPARTMENT.

Last year. 12th Nov.	Liabilities.	4th Nov., 1903.	11th Nov., 1903.	Increase.	Decrease.
£		£	£	£	£
3,177,895	Rest	3,155,233	3,171,677	16,444	...
8,637,637	Public Deposits .	6,388,706	6,226,366	...	162,340
39,264,304	Other „	40,477,251	38,923,056	...	1,554,195
136,134	7 Day Bills . . .	156,380	98,024	...	58,356
	Assets.			Decrease.	Increase.
16,416,132	Gov. Securities .	17,199,056	16,486,556	712,500	...
26,890,956	Other „	25,287,288	24,423,615	863,673	...
20,278,055	Notes	20,129,395	20,052,395	77,000	...
2,183,827	Gold and Silver .	2,114,831	2,009,557	105,274	...
				1,774,891	1,774,891
46·75 % 4 %	Ratio Bank Rate . . .	47·30 % 4 %	48·75 % 4 %	...	...

ISSUE DEPARTMENT.

Last year. 12th Nov.	Liabilities.	4th Nov., 1903.	11th Nov., 1903.	Increase.	Decrease.
£		£	£	£	£
31,164,090	Gold and Bullion	30,438,545	30,154,810	...	283,735
49,339,090	Notes Issued .	48,888,545	48,604,810	...	283,735
29,061,035	Circulation . . .	28,759,150	28,552,415	...	206,735

Those who study the figures very closely are able to guess more or less accurately what has taken place during the preceding week. For example, if we take this particular week as an illustration, we note that the reserve in the banking department has increased, which would show a lessened demand for capital. The fluctuations of this reserve, and how far the rate of interest is governed by its amount, will be discussed in a subsequent chapter.

Although the Bank issues these weekly statements, the directors do not state their reasons for making alterations. Sometimes an error of judgment occurs, but it is soon rectified, because the Bank cannot, after all, control the value of money. As the late Mr. Bonamy Price observed: "A banker is the interpreter of the forces at work, and he makes a trial of the rate which those forces prescribe".

In connection with its history, a gradual increase in deposits has already been noticed, which shows that the public have great confidence in its management.

Although there has been a gradual growth of deposits, the Bank's position in the money market as a lender of capital has materially altered. Thus, if we compare the total amount of capital lent by the Banks of the United Kingdom with that advanced by the Bank of England, we find the proportion is very small. For example, total lent by banks of the United Kingdom = £645,000,000; Bank of England = £30,500,000, or only 16 per cent. Again, its liabilities are small in comparison with the liabilities of the London joint-stock banks.

	£
Thus—1890, Bank of England =	29,000,000
„ 11 London joint-stock banks . . . =	125,539,000
1903, 10 Metropolitan banks =	229,000,000
„ Bank of England =	46,000,000

The Bank has recognised that its rate of interest does not always represent the market value, and therefore in recent years stated that, although the minimum rate was published, yet, under certain conditions, bills would be discounted below such rate.

Naturally this privilege would be granted to its own customers rather than to large financial houses which compete for bills; but such institutions avoid, in fact, making applications, if possible, since the Bank will only lend money for stated periods, and sometimes charges 1 per cent. above the published rate.

In recent years the limit for loans has been reduced from ten to seven days, but for what period the loan shall be made is a matter of arrangement.

We have noticed how the Bank by a series of events assumed a leading position in the money market, principally in consequence of large resources obtained from the Government, the London banks and from its large paid-up capital. There is, however, one important fact to be remembered, and that is, the Bank undertook to lend capital to outsiders during periods of commercial crises or panics. This was a great responsibility, and naturally the commercial world would study very closely the management of an institution which acted as a kind of trustee for the money market.

In 1825 the directors stated that the Bank had taken a firm and deliberate resolution to make common cause with the country. Mr. Hankey, a director, has stated that this opinion ought never to have been encouraged, but when we consider the unique position of the Bank of England as the holder of the gold reserve; the final resource for cash payments in this country must be this institution, and therefore must of necessity render financial assistance to the community.

During these periods of commercial disaster, the amount of capital advanced has been very large. The usual proportion of 30 to 50 per cent. of reserve against liabilities has not been kept; in fact, the reserve at one time was so low as 6 per cent.

We will illustrate this policy by giving the amounts advanced during the great crises of the present century. With an increased demand for capital, the Bank at such periods naturally charged a high rate of interest, *viz.*, from 6 to 10 per cent.

BILLS DISCOUNTED BY BANK OF ENGLAND.

				£		
1809	.	.	.	15,475,700		
1810	.	.	.	20,070,600	panic year.	
1825, Feb. 28	.	.	.	2,466,000		
„ Aug. 31	.	.	.	5,486,000		
1826, Feb. 28	.	.	.	9,597,000	} crisis year.	
„ Aug. 31	.	.	.	2,950,000		
1836, Feb. 20	.	.	.	2,900,000		
„ Aug. 30	.	.	.	4,400,000		
1837, Feb. 28	.	.	.	11,200,000	} crisis year.	Rate.
„ Aug. 29	.	.	.	5,100,000		4½ to 5 per cent.
1838, Feb. 27	.	.	.	3,200,000		
„ Aug. 29	.	.	.	2,900,000		
1846, Feb. 28	.	.	.	13,137,000		3 per cent.
„ Aug. 29	.	.	.	6,067,000		4 „
1847, Feb. 27	.	.	.	8,879,000	} crisis year.	5½ „
„ Aug. 28	.	.	.	9,163,000		5 „
„ Oct. 2	.	.	.	10,399,000		5 „
„ „ 9	.	.	.	10,978,000		5½ „
„ „ 15	.	.	.	11,907,000		
„ „ 23	.	.	.	12,492,000		8 „
1856, Feb. 23	.	.	.	8,883,000		5½ to 4½ „
„ Aug. 30	.	.	.	4,446,000		6 „
1857, Feb. 28	.	.	.	8,859,000	} crisis year.	5½ „
„ Aug. 29	.	.	.	7,893,000		8 „
„ Oct. 24	.	.	.	9,636,000		
„ „ 31	.	.	.	11,105,000		
„ Nov. 4	.	.	.	11,439,000		10 „
„ „ 11	.	.	.	13,233,000		
„ „ 18	.	.	.	16,003,000		
„ „ 25	.	.	.	17,376,000		
„ Dec. 2	.	.	.	17,788,000		

In 1857 the Bank stated that advances would only be made to bill brokers at certain periods when the public deposits were particularly large. but at other times applications for advances would only be considered under exceptional circumstances. The Bank, however, in the panic year of 1866, disregarded this rule.

BILLS DISCOUNTED.

	£	Rate.
1866, Feb. 28	7,253,000	7 per cent.
„ May 2	8,834,000	6 „
„ „ 9	9,249,000	7 and 8 „
„ „ 16	13,831,000	9 and 10 „
„ „ 23	14,501,000	10 „
„ „ 30	16,512,000	10 „
„ June 6	16,003,000	10 „

The policy of the Bank during the critical years of 1872-73 and 1878-79 has been ably defended by Mr. Birch, the late governor. He says: "In 1872-73 an enormous amount of bills were created with a view of withdrawing gold from England to assist in the payment of the French indemnity to Germany. The Bank recognised the danger which might arise from this being carried to too great an extent, and then crippling the ordinary business of the country, and rapidly raised the rate of discount. I find that in 1872 we had seventeen changes in our rates of discount; in 1873 we had twenty-four changes. The bank rate varied from 3 per cent. to 9 per cent., and from 10 per cent. to 12 per cent. was charged in the latter period on advances, not with a view of making large profits, but with a view of telling people that it was a class of business the Bank would do everything in its power to keep within reasonable bounds."

In October, 1878, came the crash caused by the failure of the City of Glasgow Bank. The Bank of England was in a good position to meet the emergency, and the

threatened crisis passed away. The rate was never raised above 6 per cent. : many thought it should have gone higher, following the precedents of 1872-73, but in doing so they did not recognise the fact that the circumstances connected with these periods were entirely different.

“In the year 1873 the stringent action on the part of the Bank was with a view to put a stop to the discounting of certain financial bills, and in the year 1878 the main object of the Bank was to avoid all unnecessary cause for alarm; and, the foreign exchanges being in favour of this country, the Bank could show a bold front to the difficulties of the situation, and did so, and I venture to think its action met with general approbation.”

This is a very important declaration on the part of the governor of the Bank, showing that its present policy is to assist the money market within reasonable limits. In the year 1890 the directors even went a step further in order to prevent a financial disaster; when the great house of Baring was in difficulties, they called a meeting of the representatives of the principal banks, and agreed with them to guarantee all the outstanding acceptances of the above-mentioned firm. This action on the part of the Bank no doubt prevented a great commercial disaster. We think the policy was possibly wise under the circumstances, but whether the Bank of England should guarantee the solvency of houses of repute when in difficulties is a question for serious consideration. A crisis might possibly have been avoided in 1866, the memorable year which witnessed the downfall of Messrs. Overend, Gurney & Co., but when a bad system of finance exists in the country it is preferable that firms who encourage reckless speculation should not be assisted. Of course, this is a somewhat different policy

from that of refusing to assist the market when it may be the means of avoiding a crisis or panic.

The Bank has in recent years made concessions to its rivals in the money market, *viz.*, the bill brokers, and agreed to discount bills for them which have not more than fifteen days to run, at not less than bank rate; but, of course, it reserves the right to charge a higher rate. No doubt this tends to make the Bank of England rate more in harmony with that of the outer market.

Although the large joint-stock banks have enormous resources, yet the position of the Bank of England is unique; in fact, no country possesses an institution wielding such power over the demand and supply of capital; and its position is closely watched in the large commercial centres of the world.

It is satisfactory to observe that its great powers have not been abused; the prosperity of this country has always been first considered rather than the payment of high dividends to its stockholders.

CHAPTER XVI.

CAUSES OF FLUCTUATIONS OF RATE.

IT is now desirable to discuss some of the forces which cause fluctuations in the rate of interest; naturally they are varied in character in a country like ours, with continual changes in the methods of trade which must alter from time to time the value of money; in fact, we might say that each year reveals some new force which may possibly have an important financial effect.

The first great cause would be the position of English trade and commerce; the trade of this country is, to some extent, transacted by means of borrowed capital obtained from the banks, which hold large deposits.

When trade is active more capital is required, therefore we should expect the rate of interest to rise; on the other hand, when depressed less is necessary for the requirements of the country.

Our imports and exports are a good index as to the state of trade; every month we see reference made in the money articles of the daily papers as to the increase or decrease of our commerce. The reports from our consuls abroad also inform us whether capital is required in various parts of the world.

When trade is active we should expect prices to rise, in consequence of an increased demand; on such occasions we get merchants anxious to take advantage of the im-

provement in prices, and increase their business by means of borrowed capital.

Again, when prices are rising, the merchant is able to borrow more capital from the banker, because of the increased value of his goods. We should also expect to notice the imports increasing with a general improvement, because other nations are also anxious to send us goods in order to obtain higher values for their commodities.

On the other hand, exports would be diminished because the rise of prices causes a less number of purchases to be made in this country for export, in consequence of the margin of profit becoming less on each transaction. Whenever there is a *great* difference between the values of imports and exports, the balance finally must be paid in gold, the only commodity which can be utilised for settling international indebtedness. Of course, one notices a great discrepancy between the values of our imports and exports, therefore one would imagine that large sums of gold have continually to be sent from this country. This, however, is not the case, since England has lent enormous sums to foreign countries, which have to remit money as interest.

Again, this country derives a large income from her carrying trade. When, however, there is no equilibrium the balance must be paid in gold, and that metal can only be obtained in large quantities from the Bank of England; this is one of the reasons why the reserve of gold at the Bank is so important, and as gold represents capital, its movements to and from this country show to some extent the supply and demand.

Another important cause is that the reserve of gold in the vaults of the Bank represents the final resources of this country for meeting cash payments: we have noticed

that the banks keep a part of their deposits at the Bank of England, and consequently there is no other large stock of gold in existence: all sudden demands must therefore be met by that institution.

Our credit system is so vast that one naturally looks to the stability of the banks which hold the surplus capital of the country; if they were called upon at any time to repay all their depositors, it would be an impossibility. The state of credit is therefore an important item in studying changes in the rate of interest.

All sudden demands for capital soon affect the reserve at the Bank of England; as we recognise in this country the importance of keeping a contingent fund, it is necessary that something should be done to protect such reserve. Fortunately, the Bank of England has a good instrument for this purpose, *viz.*, the rate of discount, and capital soon finds its way to the centre where the highest rate of interest prevails. The reserve is, therefore, of great importance, consequently it is necessary to understand how it influences the value of money.

The amount of gold held must be considered under three different aspects, *viz.*, first, the currency requirements of the country which vary considerably, and shown in the autumnal demand. In the second place we have the international demand, which is principally obtained from the Bank. There is finally the reserve of gold and notes in the banking department, which is of the greatest importance, since the rate of discount is largely influenced by it.

The daily papers refer continually in the money article to this reserve as an important factor in fixing the rate of interest for the loan of capital. To an outsider not conversant with the familiar terms used daily in Lombard

Street, the remarks sometimes made are somewhat misleading. We find reference made to the reserve of gold and notes in the banking department, and possibly in the same paragraph the bullion in the issue department is considered. It is then stated that although a fair reserve exists in the banking department, yet we must expect to see high rates, because a million or two has been drawn from the issue department.

By the Act of 1844 the Bank was allowed to issue £15,000,000 of notes against securities, since increased to £18,500,000, and for any sum issued in excess gold must be held in reserve.

It is clear that any one holding notes can obtain gold from the Bank, because that institution is compelled to pay in coin all notes presented for that purpose. How then does the withdrawal of gold from the issue department affect the value of capital?

Mr. Clare, in his excellent book entitled *A Money Market Primer*, shows the effect of a withdrawal of gold on the reserve at the Bank of England.

Thus, when a depositor withdraws £500,000, notes to that amount are taken from the reserve and returned to the issue department. These notes are cancelled, and sovereigns which are held against them are given in exchange. The effect on the balance sheet is as follows :—

ISSUE DEPARTMENT.

Notes . . .	£38·8 millions	Securities . . .	£16·4 millions
		Gold . . .	22·4 „
			<hr/>
			£38·8

Withdrawal.

Notes . . .	£38·3 millions	Securities . . .	£16·4 millions
		Gold . . .	21·9 „
			<hr/>
			£38·3

BANKING DEPARTMENT.

Capital and Rest . £18 millions	Government Securities £11·7 millions
Deposits . . . 37·2 „	Other „ 28·7 „
	Notes . . . 13·8 „
	Coin . . . 1 „
<hr/>	<hr/>
£55·2	£55·2

Withdrawal.

Capital . . . £18 millions	Government Securities £11·7 millions
Deposits . . . 36·7 „	Other „ 28·7 „
	Reserve . . . 14·3 „
<hr/>	<hr/>
£54·7	£54·7

If, however, the money market restores its balances to the former level, it borrows of the Bank of England or discounts bills at that institution.

We have already seen that gold is the final means for settling international trade, and this commodity can only be obtained in large quantities from the Bank of England.

When capital is leaving this country in the shape of gold it represents a variety of transactions—such as a scarcity of capital at a foreign centre; to pay for food imported into this country, or possibly to carry out a large financial operation.

The reserve in the banking department is the amount of notes, gold and silver held against the public, or other deposits and seven-day bills. If, therefore, we ascertain the proportion per cent. of notes, gold and silver against the said liabilities, we are able to compare the amount in comparison with the previous week, or what was held in the corresponding week twelve months ago.

In addition to the currency requirements of this country, it is necessary to keep a certain amount of gold in order to preserve the convertibility of bank notes.

We are informed sometimes that the Bank directors have decided to raise the rate, because possibly a small quantity of gold has left the Bank; whereas the actual

cause might be a depletion of the reserve in the banking department, caused by a scarcity of capital, or possibly other considerations known only to the Bank directors. Of the two reserves of which we have spoken, that of the banking department is certainly the most important in causing fluctuations in the rate of discount.

Mr. Palgrave says: "Though the total amount of bullion held by the Bank is a very important thing, the rate of discount does not appear to be regulated by it".

This is shown by the following returns:—

		£	Rate of Discount.
1844	Bullion held	13,500,000	$2\frac{1}{2}$
1845	"	15,200,000	3
1846	"	14,800,000	$3\frac{1}{2}$
1854	"	17,500,000	$3\frac{1}{2}$
1856	"	10,900,000	$5\frac{3}{4}$
1857	"	10,100,000	$6\frac{3}{4}$
1858	"	17,800,000	$3\frac{1}{4}$
1865	"	14,500,000	$4\frac{3}{4}$
1866	"	14,900,000	7
1870	"	20,400,000	3
1871	"	23,500,000	3
1872	"	22,600,000	$4\frac{1}{4}$
1903	"	30,000,000	4

We know that at times the market suffers from a scarcity of capital rather than of gold. The figures already given show that on several occasions the reserve of gold in the issue department has been low, with a corresponding low rate of interest; but there is a closer connection between the reserve in the banking department and the rate of discount.

It has been already stated that the demand for capital does affect the amount of bullion in the issue department. Capital is required to pay for the balance of trade against us, and must be finally liquidated by means of gold drawn from this department. It indicates that capital is leaving this country for the payment of food or

other necessities purchased ; but it is somewhat difficult to decide as to the amount of gold which should be retained in order to meet every contingency.

There is no doubt that the Bank is able to attract bullion from abroad, when its reserve of that commodity is low, by raising the rate.

On the other hand, we must remember that the Bank has not experienced for many years a run on its resources for gold. So long as notes can be obtained, the holders do not appear to require them exchanged. In consequence of the banks keeping their reserves at the Bank, a less amount of gold is retained in their tills, and although the liabilities of the banks have increased, yet the amount of cash held is somewhat small.

		Cash Held.
Thus—1903, 10 banks' liabilities, £230,000,000		15·0 per cent.
1879, 11 ,, ,, 125,539,000		12·8 ,,

Of course, improved communication, the use of telegraphic transfers and the great increase in the circulation of cheques have economised gold. Yet, on the other hand, a sudden demand for that metal must be met at the Bank of England, consequently we get changes in the rate of discount, due to the movements of comparatively small amounts of gold.

Sir R. Giffen estimates that with a capital of £6,000,000,000 the quantity of gold and silver held only amounts to £20,000,000, or 3 per cent.

Any increase or decrease in the precious metals must affect the value of capital, and such changes are reflected in the reserve of the Bank of England. All transactions are expressed in gold ; therefore, if we get prices rising, an additional amount must be added to the nominal capital, particularly to that represented by the loans and deposit of banks. If wages rise in this country more gold is

required; the reserve at the Bank is therefore proportionately diminished.

Our monetary system is a delicate one, and what M. de Laveleye stated in 1864 is possibly of more force at the present time. "All countries which carry on gigantic transactions with small reserves of gold and silver, and which have a vast movement of importations and exportations, must be exposed to these economical perturbations. The more a country expels the precious metals from the channels of circulation, and replaces them by instruments of credit, bank notes, cheques, warrants, deposits, clearing houses, etc., and the more, at the same time, it develops its relations with foreign countries, the more it will be exposed to the periodical return of financial perturbations, because more easily an unfavourable balance of trade and payments will disturb all the mechanism of exchange, and will require from the managers of credit institutions redoubled circumspection, prudence and ability."

We have in this country a gigantic system of credit built up on a small gold reserve, and in order to protect the same the Bank of England has very frequently to alter the rate of discount.

By raising the rate, capital is attracted from abroad, and the reserve at the Bank is replenished.

London being the financial centre of the world, other countries naturally ascertain the rate of interest in this country, since capital generally finds its way to the most profitable market.

The effect of high rates prevailing in London soon makes itself felt on the trade of this country; prices of commodities fall, and this tends to diminish imports; but, on the other hand, exports are increased, and must be paid for by means of gold.

If we study the Bank reports we shall observe that the

rate of interest is dependent upon the reserve principally of the banking department, so that with a low reserve we get high rates, and *vice versa*. This is shown from the following table :—

	Reserve.	Rate of Discount.
1845-49	£8·5 millions	£3 11 4
1850-54	9·8 „	3 5 10
1855-59	8·5 „	4 14 3
1860-64	8·4 „	4 15 2
1865-69	9·6 „	3 18 3
1870-74	12·3 „	3 10 3
1875-79	13·8 „	2 19 7
1880-84	13·4 „	3 7 7
1885-91	13·7 „	3 8 4
1897-1901	22·9 „	3 9 3

The period 1897-1901 includes the recent war in South Africa and shows us high reserves concurrently with high rates of interest.

Fluctuations in the rate of discount are therefore due to the movements of comparatively small amounts of capital. We have, as it were, all the forces which affect the money market concentrated upon the reserve of the Bank of England.

Sir R. Giffen says that “the rate of discount in the short loan market of a banking centre like London is not to be identified with the rates for loans generally, and it is only the rate for special loans between special classes of borrowers and lenders. Every change tells on the *sensitive* short loan market.”

The position of the Bank of England in the money market is that of a large dealer who fixes the price, and then sees whether customers will transact business. Outside are grouped large dealers in capital, who undersell the Bank in order to carry on their business.

These large money dealers are known as bill brokers, who obtain capital from the banks which enables them to discount bills at low rates in the market. It seems rather

an anomaly that institutions should lend capital to outsiders to enable such persons to discount bills at fine rates. The effect has been somewhat felt by the banks, who now get a less number of bills for discount than formerly ; this diminution is to be regretted, since good bills are one of the best investments for surplus capital.

A few years ago the bill brokers only discounted the acceptances of banks or of large financial houses ; but at the present time a large amount of trade bills are taken.

Bankers, however, find it convenient to lend their day to day balances to the broker, because an investment is at once found for surplus resources, and the money so lent can be called in at short notice. It must also be remembered that banks allow interest on deposits, therefore it is desirable that the capital entrusted to them should not remain unproductive.

The bill brokers either lodge bills which they have discounted as security for capital so advanced, or deposit marketable securities such as Consol Certificates, India Government Bonds, or Indian Railway Debentures. The latter class is known as "floaters," and when the loan is called in, the banker returns such hypothecated securities.

As the bills which are lodged as security mature, they are replaced by others having a longer time to run.

The position of the bill brokers is, however, one of great delicacy, because they are somewhat dependent upon the banks for the greater portion of their funds. If the banks have no surplus capital to lend, the brokers apply at the Bank of England for loans, in order to meet their requirements. However, they always endeavour to avoid making applications at the Bank, since only loans can be obtained for stated periods, and it is manifest that within a week great fluctuations might occur in the value of money.

No doubt this system of lending capital to the bill brokers has an important effect upon value, which is shown in the daily quoted price. We sometimes notice the bank rate 5 per cent., whereas the market rate is only 3 per cent.; if the Bank finds its discount business getting less, the rate is lowered in order to bring it more in conformity with the market. The Bank certainly does affect the rate for money at a particular moment, but it cannot affect the average rate.

“The reason is that any momentary fall caused by the caprice of such a bank tends to create an immediate rise, so that upon an average the value is not altered.”

There is, therefore, no ground for believing that the price of capital is governed by different laws than that of supply and demand, in fact, like any other commodity.

We have already stated that both the demands for the internal and foreign trade of this country are reflected in the reserve of the Bank of England. With regard to the foreign trade, we are able to understand the position of the market by means of the foreign exchanges. These tell us whether a demand for capital exists in any of the great financial centres of the world; all the forces which affect the supply and demand are exhibited in such exchanges.

Again, international payments for goods exported or imported are made by means of drafts or bills drawn upon banks or large mercantile houses in order to avoid the shipment of gold, and this competition for such documents causes fluctuations in the foreign exchanges.

The following table shows us the extreme points when gold is likely to reach this country, or the reverse, from the three great financial centres:—

Paris	25·32½ = 4 per mille for us.
„	25·22½ = par of exchange.
„	25·12½ = 4 per mille against us.
Berlin	20·52 = 5 per mille for us.
„	20·43 = par.
„	20·33 = 5 per mille against us.
New York	4·89 = 5 per mille for us.
„	4·867 = par.
„	4·827 = 8 per mille against us.

The par of exchange is the identical value of the sovereign expressed in its foreign equivalent.

The extreme fluctuations of the exchange are known as bullion points, because when the rates reach these points gold would be shipped either to or from this country. However, it is possible for the rates to rise or fall beyond such limits, because on the shipment of gold a saving might be made on freight, insurance or other charges. One mercantile house might be in a better position than another to secure better terms for consignments abroad.

Our trade is continually shifting from one place to another; a fresh demand for capital springs up in one corner of the globe, followed possibly by a diminished use of it in another. All these movements of capital react upon the price of commodities, and in their turn affect the foreign exchanges.

Many years ago the Bank directors considered them as their principal guide in fixing the rate of discount, but in recent years the demands for capital by the Stock Exchange are possibly of more importance.

Mr. Birch says: “The great thing which governs us is the enormous transactions on the Stock Exchange in France, in Germany and in the United States. These are the operations we have to follow most carefully.”

All such demands would affect the reserve of the Bank of England. The following figures will give us some idea of the demand for capital by the Stock Exchange:—

In 1889 there were registered 2,788 companies, with a capital of £241,277,000, the largest number ever known, exceeding the previous year by 238; but they were not all floated.

Since the Companies Acts were passed 83,915 companies have been registered, with a capital of £3,740,520,000. There are now 33,259 companies in existence, with a capital of £1,805,140,000.

Sir R. Giffen has estimated the capital of the country to be £15,000,000,000; we observe that the figures for 1889 were very large, *viz.*, about one-seventh of the present amount. Although it does not represent capital paid up, yet the amount is enormous.

Some of this capital would be sunk in railways, mines, docks and kindred undertakings, which could not be reproduced for a long term of years.

When there is a great increase in the number of joint-stock companies, it may happen that the savings of the country are not sufficient to meet the great demand, and then the value of money must be high. Shareholders are unable to pay their calls without the assistance of banks, consequently the rate of interest rises.

Again, there are fluctuations due to the increased demand for capital in order to meet the requirements of trade, and lastly there are changes which occur annually; of these periodical movements the most important is the autumnal demand, which is principally a currency requirement.

The cause of this demand is, that after the ingathering of the harvest a great number of transactions take place; corn is sold and other commodities are purchased, which tends to an absorption of capital.

The weekly returns of the Bank of England for the third and fourth quarters of the year show the result of

these transactions in a marked decrease in the bullion and loanable capital.

There is also the autumnal demand for gold from Scotland, due to the fact that rents, salaries, etc., are paid on the Scotch quarter day, *viz.*, 11th November.

At this period of the year the Scotch banks exceed their authorised issue of notes, and they are obliged by the Act of 1845 to hold gold in reserve against any excess. After the demand has subsided, this hypothecated gold soon finds its way back to the Bank of England.

Professor Jevons speaks of the autumnal demand as follows : “ To sum up, then, the October drain is due, like many others, to economic disturbances, to a concurrent of causes. The dispersion of money in wages during the summer, and the absorption of money and capital in buying up the produce of the harvest, occasion a general autumnal drain upon the resources of the banks, causing the private deposits, the bullion and the reserve of notes to fall. Then the general quarterly payment of rents, bills, and especially the dividends at the beginning of October, cause a sudden extra run upon the resources of the banks, quite sufficient in many states of the money market to engender a panic, unless, indeed, its normal and temporary nature be well understood. The result of this autumnal demand is that we find the value of money higher for the last six months of the year.”

This was illustrated by the following analysis of bank rates :—

						Average Rates.
1845-61	.	.	January to March	.	.	3·97 per cent.
„	.	.	April to June	.	.	3·87 „
„	.	.	July to September	.	.	3·60 „
„	.	.	October to December	.	.	4·17 „

The same effect still takes place—the last six months generally showing a higher rate of discount.

The Bank of England pays the interest on the National Debt by quarterly instalments on 5th January, 5th April, 5th July and 5th October. The result of these payments is shown in the weekly balance sheets :—

- (1) A rapid decrease in Government deposits.
- (2) A decrease in the reserve of notes.
- (3) A decrease in the private securities.
- (4) A slight decrease in the bullion.
- (5) An increase in the private deposits.
- (6) An increase in the note circulation.

When the dividend money, now about £3,675,000 per quarter, is released, it has the effect of increasing the supply of capital, consequently at these periods we may expect the rate of interest to fall.

The financial requirements of the Chancellor of the Exchequer frequently cause changes in the value of money. This is especially the case when there is a large sum floating in the market in the form of Treasury or Exchequer Bills. The repayment or renewal of such obligations has an effect upon the rate of interest, especially at times when capital is scarce. The rates at which these obligations are renewed would be an indication to the Bank directors as to the position of the outside market.

In the financial papers reference is made to certain payments or calls which fall due. For example, an instalment on an Indian loan of say £1,000,000 has to be paid, consequently the market is denuded of that amount of capital. Again, a large company makes a call upon its shareholders, who are obliged to find capital to meet the same ; then, at the same time, we might have the Government borrowing £1,000,000 on Treasury Bills, which are issued at various dates, and if they are applied for at a low rate of interest, it would indicate that the market expects a low average rate for money.

The result of such calls upon the market would be to raise the rate of interest.

We often see it stated that the Bank of England has been borrowing on stock, which means that capital is obtained in the market by the same methods as the bill brokers. The weekly reports show this by a decrease in Government securities; this is done in order to make the rate more effective, or, as it is stated, to get control of the surplus in the market.

It is difficult to understand how such capital can be utilised at a profit, but when the Bank gets control of the market it is able to obtain more discount business, which no doubt would more than compensate it for the amount paid as interest on loans.

The rates for money prevailing on the Stock Exchange form a guide to the Bank directors in fixing their rate, and they study closely the events which are taking place in the great market for securities.

A large portion of the business transacted on the Stock Exchange is of a speculative nature. Stock is purchased, but not paid for; so that when the fortnightly settlement arrives, the buyer has to obtain a loan on his stock, or, as it is termed, "carried over" to the next settlement. This is done by the broker, who charges his client interest for the transaction; the rate charged affords some indication as to the scarcity of capital or otherwise.

We have been considering some forces or economic causes which tend to increase the value of capital in the market. There are, however, causes which have the effect of lowering the rate of interest.

Sometimes a large Government loan is paid off, which has the effect of placing more capital on the market; again, a railway is purchased by a Government, and the capital returned to its shareholders. This occurred when the

Dutch Government purchased the Dutch Rhenish Railway, and some effect was produced upon market rates. We have, in fact, rates continually changing in consequence of the movement of comparatively small amounts of capital.

However, for more permanent causes of annual average rates, whether high or low, the condition of trade is the most important factor. When trade is depressed, less capital is required, and therefore years of depression would mean low average rates of interest.

Our commercial system is highly organised ; the division of labour has made trades dependent upon each other ; a depression in one soon affects another, and this reacts upon the banks, which find that less capital is required, consequently rates for money fall.

Again, we find credit an important factor in the money market, not only in connection with the mercantile community, but also with banks. Trade is carried on by means of borrowed capital obtained from the banks, which lend their deposits.

A greater portion of the resources of banks is utilised in the discounting of bills which represent credit transactions ; we have seen that the term discount is used in the money market rather than the term interest, showing that the purchase of these credit documents is the most important business in the money market.

We have already stated that the Bank is only in the position of one of the largest dealers in capital. We must, therefore, consider the action of the other lenders, especially the bill brokers and large discount houses, who are a great power in the market. These institutions compete against the Bank in order to obtain capital and to utilise the same in the discount of bills.

For example, the effect of this competition may be seen

by the following quotation of rates prevailing at one time in the market, *viz.* :—

Market Discounts.		Bank and Money Rates.	
	Per cent.		Per cent.
60 day bills . . .	$3\frac{7}{8}$	Bank rate . . .	4
3 month bank bills .	$3\frac{7}{8}$	Bank of England loans .	$4\frac{1}{2}$
4 " " " "	$3\frac{7}{8}$ $3\frac{1}{2}$	Bankers' deposit rates .	$2\frac{1}{2}$
6 " " " "	$3\frac{1}{4}$ $3\frac{1}{2}$	Brokers' deposit rates .	3
3 " fine trade bills .	$4\frac{1}{2}$	" notice . . .	$3\frac{1}{4}$
4 " " " "	$4\frac{1}{2}$	7 day market loans . .	3 $3\frac{1}{2}$
6 " " " "	$4\frac{1}{2}$ $4\frac{3}{4}$	Day to day money . . .	$1\frac{1}{2}$ $2\frac{1}{2}$

The above rates tell us somewhat as to the position of the money market; we note that the rate for three-month bank bills differs only $\frac{1}{8}$ per cent. from the official rate; this would indicate that the Bank is able to effect some discount business, and that its rate conforms to the market value for capital.

The rate for six-month bank bills is a fraction less, because the market assumes that the average value of money for that period will be less.

It will be noticed that the rate for fine trade bills is a little more, *viz.*, from $\frac{1}{4}$ to $\frac{1}{2}$ per cent.; this additional interest is charged because more risk attends the discount of trade bills than bank acceptances, which will almost for a certainty be paid.

We observe that the Bank charges $\frac{1}{2}$ per cent. above the published rate for seven-day loans. This is the usual custom of that institution; therefore every dealer in money endeavours to meet his engagements without its aid.

The banks generally allow $1\frac{1}{2}$ per cent. below bank rate for deposits, except when very low, when there is only a difference of 1 per cent. Recently, we have seen the rate for deposits allowed by the banks lowered to $\frac{1}{2}$ per cent.; whilst the Bank of England remained at the nominal rate of 2 per cent. This would show the great difficulty experienced in utilising deposits at a profit. The cause of

this difference between discount and deposit rates is that the banks have at times to lend money at call much below bank rate. Then, again, an investment for depositors' money must be found, which of necessity entails risk, therefore some margin is required as an insurance fund. We note that day to day money is only worth $1\frac{1}{2}$ to $2\frac{1}{2}$ per cent.; therefore, if a banker allowed $2\frac{1}{2}$ per cent. on deposit, there would be a loss on deposit money lent at call. However, it is the *average* rate which must be considered.

The brokers' deposit rate is a little higher than the banks', *viz.*, $\frac{1}{2}$ per cent., which would indicate that they are anxious to secure the use of capital, and consequently will pay a higher rate.

The brokers prefer a low average rate rather than a continually fluctuating one, in order to transact business. The profit of the brokers would be shown in the difference between their allowance for deposits and the market rates for discount. They also allow an additional $\frac{1}{4}$ per cent. for money lent them for seven days, in order to avoid applications to the Bank of England.

The last quotation is for day to day money, which represents capital that may be called in at any moment by the banks. Naturally money borrowed on such conditions is not so valuable to the broker, because, if loans are called in, he is obliged to borrow elsewhere, and it is difficult to foretell what the requirements of the market will be on the following day.

By studying these rates we get an insight into some of the forces which cause fluctuations in the value of capital. The tendency in the money market is towards an equalisation of rates, and naturally every borrower endeavours to find the cheapest market. When bills of a certain class are discounted at the banks, it is in consequence of the

holders not being able to discount them at market rates: although their credit is good, yet they are not sufficiently known in the market. The forces at work in the market are always tending to make the bank and market rates equal. When there is a great discrepancy between the two, a less number of bills are discounted by the banks; some of the large institutions, however, compete for bills; that is, they discount for their customers at market rates, and such banks would not experience the above-mentioned result.

Again, London banks soon ascertain how rates of interest are tending, by the daily applications of the brokers. When capital is scarce in the market, the bill brokers call two or three times a day in order to obtain the surplus capital, and offer at times even higher rates than the market quotation, in order to avoid applying to the Bank of England for loans.

CHAPTER XVII.

EFFECT OF CHANGES IN RATE.

HAVING briefly considered the cause of changes in the rate of discount, we will now study some of the results. Of these the most important would be its relation to the commerce of this country, since, as we have seen, the greater part of our trade is carried on by means of borrowed capital.

Every change in the price of money must of necessity react upon the value of commodities; merchants purchase goods on the presumption of being able to borrow capital at all times, and if borrowing becomes difficult or disorganised, the whole trade of the country suffers. Of course, profits made on the purchase or sale of goods are considerably affected by fluctuations in the rate. If a merchant has to pay a higher price for the loan of capital than he has estimated in a contract, his profit might be reduced to nothing.

Trade would become restricted if they were abnormally high, because merchants would find it difficult to obtain a correspondingly higher value for their commodities.

If, however, we get low rates of interest, production would be stimulated, and, as a consequence, trade becomes active; but a high rate does not materially affect commerce, although great fluctuations may be detrimental.

A high rate would stop speculation, and this at times is beneficial to the country; it would also be the means of preventing a certain amount of circulating capital being

converted into fixed ; that is, expended in the construction of railways, mines, docks and other similar undertakings, and in such cases capital would not be reproduced for a long term of years.

We find reference made in financial journals as to the price of capital in relation to trade ; they inform us that at times the rate of discount should be reduced in order to afford relief to the mercantile community. This demonstrates how closely the trade of this country is associated with the value of money.

The late Mr. Bagehot has stated that “ Lombard Street is by far the greatest combination of economical power and economical delicacy that the world has ever seen ”. It is the centre, or the money market, of the whole world ; all demands for capital are supplied from this centre.

If a Foreign Government wishes to borrow capital, the rate of interest prevailing in Lombard Street is generally first ascertained. If high, the Government would wait for a more favourable opportunity—every nation wishes to borrow cheaply, therefore avoids a market where money is dear.

The English market has been invariably a cheap one for borrowers, and therefore foreign States have found it advantageous to borrow here, rather than in Paris, Berlin or New York.

This is seen from the average rates since 1845 :—

						£	s.	d.
1845-54	.	.	.	.	.	3	8	8
1855-64	.	.	.	.	.	4	14	8
1865-74	.	.	.	.	.	3	16	5
1875-84	.	.	.	.	.	3	3	8
1885-94	.	.	.	.	.	3	3	2
1895-1902	.	.	.	.	.	3	2	9

The rate of interest allowed by the banks for money on deposit is determined by the bank rate. The London

banks generally allow $1\frac{1}{2}$ per cent. below bank rate, unless the rate is very low, when there is only a difference of 1 per cent., and it has been explained elsewhere the reason of this difference. The various banking institutions and discount houses announce in the daily papers their deposit rates the day after the bank rate is fixed by the Bank of England.

If a high rate of interest is allowed, we should expect to see the deposits in banks increase, but if low they would tend to decrease, because the depositors would naturally find other investments for their capital. It may, however, happen in consequence of the difficulty of finding employment for capital, and possibly through a want of confidence, the deposits in banks may increase, although the rate allowed is only $\frac{1}{2}$ per cent.

The value of money in the London market soon affects the rates prevailing in other great commercial centres, such as Paris, Berlin, Vienna, Amsterdam and New York. The changes in the bank rate are soon reflected in the foreign exchanges; thus, with a high rate prevailing in the London market, we should naturally expect to see the exchanges gradually tend in favour of this country. This is in consequence of capital being sent here for investment.

It might be said that London is the great clearing house of the world; more bills of exchange are drawn upon London than any other commercial centre, and such bills are a favourite investment on the Continent, because the holders can profit by the variation in the rates of exchange.

Lord Goschen refers to this subject in his book on the foreign exchanges, thus: "We now come to the fact which it is very important clearly to appreciate, that at any moment there is in the hands of bankers and exchange dealers a large amount of bills on foreign countries, held partly for the purpose of speculating on

a rise or fall in the price of bills, but to a very large extent solely for the sake of the interest which is to be made on them. Bills on England, owing to the high rate of interest which they often bear as compared with continental rates, are a favourite investment abroad. In Paris, Berlin, Frankfort, Hamburg and other continental cities, the bills on England held by bankers and joint-stock companies often amount to many millions sterling, and a very large sum remains in their hands for several months; in fact, from the time when the bills are drawn to the time when they fall due."

The changes in the rate of discount have a considerable effect on the Stock Exchange, where vast amounts of capital are lent fortnightly, consequently such changes soon affect the value of securities. If rates are low, speculation increases, and more purchases are effected; various stocks are bought because the rates of interest on such stocks are higher than that which borrowers pay to the banks.

Supposing £10,000 Colonial Stock is purchased, and the stock bears 4 per cent. interest, and $2\frac{1}{2}$ per cent. is paid for the loan of capital advanced on it, then the purchaser gets $1\frac{1}{2}$ per cent. by the transaction if he is able to borrow from one settlement to another.

Again, a low rate encourages speculation, because, the brokers being able to borrow cheaply, there is a tendency for stocks to be purchased, and consequently rise in value.

The rates charged for "carrying over" stock on the Exchange fluctuate with the bank rate of discount; if such rates are high, speculation is checked, and the price of securities falls. There is, therefore, a close connection between the rates for money and the price of securities.

We will briefly consider the effect upon some of the securities quoted on the Stock Exchange. At the head

of such securities would be British Government Funds, which are particularly sensitive to changes in the rate of interest, as such stocks form a floating security in the money market. The large financial houses are able to borrow capital from the banks against Consols, and, if the average rate of interest in the market is higher than the rate charged on Consols, there would be a tendency for the price to fall. The holders would prefer selling their stock and lending capital in the open market.

If, again, the banks offer a high rate of interest for deposits, the holders of Government Stock might prefer selling to get a better return. With a high market rate prevailing, the banks would be inclined to sell Government Stock in order to lend the proceeds to bill brokers, and thus secure a more remunerative return for their capital.

Again, the price of Treasury and Exchequer Bills is largely affected by the market rates for money. These securities, like Consols, are utilised by discount houses as cover for advances made by banks to such institutions. We therefore find the price of these securities fluctuating with the market value for capital.

Sir R. Giffen refers to this as follows : " There is a close connection between the short loan and the speculation in securities. The funds of the short loan market are employed partly in holding securities, and where these funds are diminished or increased from any cause, however temporary, there is an immediate effect on the price of some securities. But the great mass of securities will only be affected by more permanent changes in the rates obtainable for money in other markets."

In recent years the connection between the Stock Exchange and the banks has been of a more intimate character. As an illustration of this the *Economist* stated

that in 1889 an additional amount of £9,000,000 was lent by the banks on the Stock Exchange. The great increase in stocks now quoted has considerably increased the amount of capital which is lent in this manner.

Large amounts of stock are deposited with the banks by stockbrokers against capital lent for the fortnightly account, a certain margin being provided to cover contingencies. When the settlement arrives, a fresh loan is made, and the stock is carried over for another fortnight. It is easy to understand how the rates for money must affect the price of securities which have not been absorbed by the public, and therefore do not represent actual purchases or sales.

Credit is also an important force in connection with the Stock Exchange. If at any time a rumour gets abroad that the banks intend to refuse loans on certain securities, the price of the same falls considerably. The withdrawal of loans by the banks from the Stock Exchange would have a most disastrous effect; it was stated some time ago that certain banks intended curtailing their loans, and even this rumour almost created a panic.

Again, any increase in the value of money would tend to increase savings, and as a large portion of such savings would be invested on the Stock Exchange, prices would therefore rise. On the other hand, a low rate of interest would act as a check on savings, and the result would be reflected in the price of securities.

The value of money in the market does therefore exercise a great influence upon all interest-bearing securities.

CHAPTER XVIII.

THE MONEY MARKET.

WE have described some of the forces which from time to time cause fluctuations in the rate of interest; the daily papers give us some account of what is really taking place in various parts of the world, in order to ascertain whether there is any probability of an increase in the value of money. The writers endeavour to ascertain whether the Bank of England rate will be raised or otherwise, by reference to the various demands for capital, especially for gold, which is the final method for settling international indebtedness.

The following extract from the *Standard* gives an excellent account of the money market :—

“11th November, 1903.

“The money market to-day was entirely dominated by the position of the New York Exchange, the withdrawals of gold on American account and the uncertainty as to an immediate change in the bank rate. Thanks to the recent payment on Transvaal scrip, and the borrowing by the market, the market is now dependent upon the Bank, to which discount business to-day was almost entirely confined, and a fairly large number of short-dated bills were taken there.

“In the open market brokers quoted the rate 4 per cent., subject to a rise in the official rate, or $4\frac{3}{16}$ to $4\frac{1}{4}$ per cent.

outright. During the earlier hours there was a tendency to quote slightly easier rates for three-month bills, and the 'yearling' Treasury Bills allotted yesterday were dealt in at about $3\frac{5}{8}$ per cent. Later in the day, however, the tone hardened on the definite announcement that bar gold had been taken from the Bank for the United States. It was generally reported that the price asked for eagles was prohibitive, and that bars were consequently sold at something like £3 18s. 0 $\frac{1}{4}$ d. Late this evening a still further sharp decline occurred in the American Exchange, and it seems likely that more gold will be taken out before the end of the week. Since the last return the Bank has sent abroad on balance over £600,000 in gold; but, on the other hand, cash has probably come back from circulation, so that no great shrinkage is looked for in the reserve tomorrow. Last week it stood at £22,244,000, and these figures in themselves would seem scarcely to justify a 5 per cent. rate. It may be interesting to recall that the last occasion when the rate moved from 4 to 5 per cent. was in January, 1901, when the reserve stood at £16,211,000.

"It must not, of course, be forgotten that the period of the year is different, and that during the last six weeks of 1902 the Bank lost over £5,000,000 in gold, and that without any withdrawals for the United States. On the other hand, there is the fact to be borne in mind that the gold arrivals each week from the Cape are much larger than a year ago, while the foreign exchanges, with the exception of New York, are moving favourably to this country.

"Before 1901 the bank rate stood as high in 1899 as 6 per cent., with a reserve of over £20,000,000, but on that occasion it was a question of the foreign bank rates—notably the German—also standing at an abnormally high

level. Before that date, one has to go back as far as 1893 for a 5 per cent. rate, when the reserve was down to £15,000,000. At the present time the official rate here is at the same level as Germany, and 1 per cent. higher than in France; while market rates of discount, as will be gathered from the table elsewhere, are well above the quotations current at all the Continental centres.

“ The position of the Bank directors in determining the present course of action is in many respects a peculiarly difficult one. The imperative nature of the demands for gold on New York account has to be recognised, as well as the fact that they coincide with probable further demands for the metal for Egypt and South America; while, as explained in our last issue, there seems reason to suppose that the Bank of France will be disinclined to part with the metal freely.

“ On the other hand, the position of investment markets and conditions of trade make it distinctly desirable that abnormally high rates of interest should be avoided, if possible; nor would it be advantageous for Continental capital to be unduly attracted to the bill market here. Owing to the relatively high rates of discount here, as compared with those current on the Continent, the situation is so far simplified that there seems no reason to apprehend the withdrawal of Continental money, even when allowance is made for the new Credit Foncier Loan, possibly to be issued in Paris this month. Doubtless the directors at their meeting to-morrow will be guided by the position of the American Exchange and their knowledge as to further gold requirements from that quarter; but, unless it is known that such demands are likely to be large, the retention of the present rate of discount for another week, or an advance to only $4\frac{1}{2}$ per cent., would seem to be justified. This latter course, indeed, would probably

prove sufficient in itself as a protective measure now that the Bank adopts the policy of charging $\frac{1}{2}$ per cent. above the official rate, so far as its loans to Lombard Street are concerned.

“ Short loans and weekly advances were in strong demand to-day, and from $3\frac{1}{2}$ to 4 per cent. was readily paid for day to day money during the earlier hours ; but in the afternoon supplies became more plentiful, owing to the discount business at the Bank, and advances over the night were finally made at about 3 per cent. A fair amount was called in by the India Council, and weekly loans were in good request at $3\frac{3}{4}$ to 4 per cent. Continental exchanges on London moved favourably, the Paris and Berlin cheque rates advancing to $25\cdot18\frac{3}{4}$ and $20\cdot45\frac{3}{4}$ respectively. Substantial gains also occurred in the Vienna and Dutch rates.”

With reference to these remarks it may be observed that no alteration in the rate of discount was made by the Bank directors ; the strong reserve held no doubt was an important factor in settling the question of an alteration.

In order to understand how the money market is affected by various economic causes, the financial history of the year 1890 will be reviewed, because it was not only a memorable year, but the cause of great anxiety to the banking community. It also affords a practical illustration of some of the forces which cause fluctuations in the rate of interest.

This year was an anxious one for the banks of this country, and, as the action of the Bank of England was somewhat criticised, we shall be able to judge to what extent the policy of the directors was correct. Each year has some leading features which distinguish it from the preceding one. Thus, the failure of the City of Glasgow Bank in 1878 had an important effect upon the market,

and the gigantic speculation in copper in 1889 was felt considerably in the financial world.

Again, the requirements of a foreign country in order to place its currency on a satisfactory basis, which may lead possibly to a drain of gold, have caused great changes in the value of money. In fact we might almost say that the requirements of the world for specie are supplied from Lombard Street.

The year 1890 opened with a bank rate of 6 per cent., and also with the outside market denuded of capital, the Bank return showing that the market had borrowed £7,000,000 to £8,000,000. This was an indication of the Bank of England obtaining control over the outside market; therefore little competition existed between the Bank and the said market. In fact, there was a deficiency of surplus capital, in consequence of the heavy calls upon the resources of the market in previous years, which have been described as mania periods. Thus, in 1888 £160,000,000 of capital was invested in South American securities, and in the succeeding year £190,000,000 of capital was subscribed for breweries, mines and trust company investments. These facts somewhat explain the position of the market throughout the year; the consumption of capital has been larger than the supply.

Sir R. Giffen has estimated the annual savings of this country to be £150,000,000, but of this amount a large portion would be invested in stock, premises, machinery, land, etc., but a balance of £80,000,000 can be regarded as free savings which require to be invested through the medium of the Stock Exchange. If, as he says, an additional £20,000,000 were added any one year the effect would be an inflation in the prices of securities, and paper profits largely increased.

By means of these instructive figures we are able to

ascertain whether the capital required for new undertakings is in excess of the annual accumulations. In order to show this we will take the capital called up for ten months to October, 1889, in comparison with the same period of 1890 :—

October, 1889, called up	£128,670,798
„ 1890 „ „	104,729,709

From these amounts we should have to deduct the amount of capital returned to this country by means of redemption drawings, but after making allowance for this return of capital, the figures given are very large in comparison with previous years.

For example, new issues of Colonial Government Municipal Loans for preceding years were as follows, *viz.* :—

1876	£25,600,000
1883	48,700,000
1884	48,900,000
1885	51,700,000

We must therefore conclude that during the previous three years the amount of capital subscribed for new undertakings had been in excess of the annual savings. The above facts clearly show why a 6 per cent. rate was prevailing in January.

The first relief which the market obtained was through the payment of dividends on Government Stocks on 5th January, amounting to £5,250,000; these quarterly payments on Government Stocks are always taken into account by the money market, and naturally tend to ease rates.

In the first quarter of the year there is another force at work which must not be forgotten, and that is the collection of taxes for the revenue. As the financial year ends on the 5th April, the collectors of taxes make strenuous efforts to obtain payment of all outstanding amounts. The revenue receipts for the quarter are about £35,000,000,

and if the Chancellor of the Exchequer lends any of this amount, it would tend to lower rates.

The action of the Government in the money market must not be forgotten in considering fluctuations of the rate of interest; it may borrow on Treasury Bills, and, whenever they are paid off or renewed, we may expect to witness some changes in money rates.

Every week we find reference made to the bank and the market rate for interest, and sometimes when there is a great difference between the two, the Bank of England endeavours to make its rate more effective by borrowing in the outer market. This is effected by borrowing on stock, which denudes the market of surplus capital. If we study the weekly balance sheets of the Bank of England, this result is shown in a decrease of Government securities.

For example :—

October 29	.	.	Government securities	.	.	£16,133,500
November 5	.	.	"	"	.	15,498,500
						<hr/>
Decrease	.	.	.	.	.	£635,000

This amount, *viz.*, £635,000, would represent the amount borrowed in the open market by the Bank.

Another important element to be remembered is the rates for money prevailing at places abroad where capital is concentrated. Such rates are quoted weekly in the following form, *viz.* :—

Paris	.	.	.	.	.	.	+	$1\frac{9}{16}$	per cent.
Berlin	.	.	.	.	.	.	-	$\frac{1}{4}$	"
Amsterdam	.	.	.	.	.	.	+	2	"
New York	.	.	.	.	.	.	-	$2\frac{1}{2}$	"
+ (above) - (below) London rates.									

The foreign exchanges are also an indication as to whether capital is likely to reach this country or otherwise. For example, we find a quotation as follows, *viz.* :—

France	+ 1 $\frac{3}{4}$ for us
Germany	- 2 $\frac{1}{4}$ against us
Holland	- 3 $\frac{1}{8}$ against us
New York	- 4 against us

As a rule, the foreign exchanges follow the changes of the bank rate, rather than precede them.

The Bank of France is able to retain gold by charging a premium; therefore high rates of discount prevailing here are unable to attract that commodity if that institution wishes to maintain its reserve.

As we have already discussed the composition of the reserve at the Bank of England, it will only be necessary to study the changes which occurred.

The stock of bullion and the reserve in the banking department in January were both low in comparison with previous years.

Thus :—

31st Dec., 1879.	5th Jan., 1887.	5th Jan., 1888.	2nd Jan., 1889.	1st Jan., 1890.
£27,601,000	£19,307,000	£20,164,000	£19,366,000	£17,782,000
Proportion of reserve to li- abilities.	30 $\frac{5}{8}$ per cent.	38 per cent.	29 $\frac{1}{8}$ per cent.	27 $\frac{1}{2}$ per cent.

There were other indications showing the expenditure of capital; for example, the clearing house returns, which are always studied by the market, since they illustrate to some extent the condition of business in the country, because capital, like every other commodity, finds its way to the most profitable market.

Of these returns the fourths of the months give us some idea as to the amount of bills in circulation, whereas those of the fortnightly settlements and the Consol settling days on the Stock Exchange show in some degree the amount of speculative and investment business of the country.

If the returns were falling off, it would indicate that less capital is required to carry on business, and we

should expect to see a gradual reduction in the rate of discount. But for the year 1889 there was an increase of £654,878,000, which indicated that capital was in great demand.

The high bank rate at the beginning of the year had the effect of turning the foreign exchanges in our favour. For example :—

	4th Jan., 1890.	11th Jan., 1890.
French Exchange	1½ for us	1 for us
German	2¼ against us	par
Dutch	3½ „	2¼ against us
New York	4 „	par

In the early part of the year the market was affected by a financial transaction which frequently occurs; in order to effect the conversion of the Russian Debt from 5 to 4 per cent., it was desirable to accomplish it when rates were low. An artificial ease was created by means of importing £1,000,000 of gold; such additional capital would temporarily affect prices.

The note circulation of March generally shows a contraction of £2,000,000 to £3,000,000 in consequence of money being required for revenue purposes. Although a 6 per cent. rate prevailed in the market, yet it had not the effect of attracting gold to this country, although the Bank of England paid a halfpenny per ounce more for bar gold in order to draw capital from abroad.

The rate was, however, reduced to 5 per cent. on 20th February, in consequence of an increase in the bullion at the Bank, and also because the reserve showed a proportion of 50 per cent. to liabilities.

When the rate is high, traders in this country suffer somewhat, because most of the banks are guided by it in fixing their charges. It is therefore of importance to the trading community that a high rate should not exist when the reserve is abnormally high.

On 5th March the rate was reduced to $4\frac{1}{2}$ per cent., the market rate being $3\frac{1}{8}$ per cent. There was, however, very little in favour of cheap money, because there were several calls due on new undertakings, and at the same time the business of the country showed some improvement; however, the rate was reduced to 4 per cent. on 12th March, in consequence of an increase to 51 per cent. in the Bank's reserve.

As we have already remarked, there is a close connection between the banks and the Stock Exchange, and all applications for new capital affect the rate of interest.

The following table shows the increase from 1885 to 1890 :—

	£	One Quarter.
New capital applications .	30,240,000	1890
“ “ “ .	56,800,000	1889
“ “ “ .	34,600,000	1888
“ “ “ .	21,500,000	1887
“ “ “ .	26,800,000	1886
“ “ “ .	13,759,000	1885

The quarterly dividends, due 5th April, would affect the market in the same way as in January, and consequently the rate was reduced on 10th April to $3\frac{1}{2}$ per cent.; the reserve at the Bank being in the proportion of $43\frac{1}{3}$ per cent. There was a further reduction, 17th April, to 3 per cent., the reserve then being $45\frac{1}{4}$ per cent. This ease, however, was not prolonged, because we find that in the following week a withdrawal of gold on balance of £357,000 had taken place, and the reserve had fallen to $44\frac{1}{2}$ per cent. Of this gold £200,000 was shipped to Buenos Ayres, where financial difficulties existed. The market also expected that the Russian Government would send its surplus capital from London to Paris, where most of its securities were held. This withdrawal of bullion had the effect of hardening market rates, especially when it was known that

gold would also be required for Scotland in the following month, *viz.*, May, in order to meet payments due on the Scotch quarter day.

The Bank of England returns for 1st May emphasised the fact that the market was short of capital, because applications for loans had been made at that institution. This was shown by an increase in the other securities of £1,358,000. Again, the Government had issued £1,500,000 of Treasury Bills, and this would cause the withdrawal of surplus capital from the market. On the other hand, low rates might be expected, because it was known that £2,000,000 of Treasury Bills, falling due at a later period, would not be renewed.

The market at this time was somewhat affected by speculations in silver; this was in consequence of the United States authorising the coinage of an additional amount. The sudden rise in the price of that metal naturally followed, and the price of all silver securities rapidly rose, it being stated that several large financial companies had speculated largely in such stocks.

The result of the silver legislation in the United States would be a reason why gold should leave that country and increase the stock here. This is in accordance with Gresham's law, which states that if two metals are used as a currency, the one of less value will remain, whilst the other is exported.

It may also be observed that the high bank rate in January and February had affected the value of securities quoted on the Stock Exchange, because 7 per cent. had been charged at that institution for loans.

On the other hand, United States securities had risen considerably in consequence of the silver legislation. However, a few months later a reaction occurred, which

showed that any attempt to give an artificial value to silver must fail.

With regard to the Stock Exchange, the cause for anxiety was the state of affairs in the Argentine Republic, where £150,000,000 of English capital had been invested. This would naturally affect banks and their rates of interest, especially as it was estimated that £9,000,000 of additional capital had been lent on the Stock Exchange.

There was nothing, however, to show that a great stringency would take place in the autumn, although the reserve of gold in the Bank was £1,000,000 less than in the previous year. In fact, it was predicted that no great drain of gold would take place in the autumn, but if we remember the vast amount of new undertakings which had absorbed the floating capital in the market, we cannot wonder at subsequent events.

The return for 12th June showed a reduction in the reserve to $41\frac{7}{8}$ per cent. The bullion in the issue department was also low, *viz.*:—

Last year	£22,884,000
June 12, 1890	21,760,000

The Indian Council at this time called in money lent on the market, and the demands for loans from the Stock Exchange were large, the market rate being only $\frac{1}{4}$ per cent. below the official quotation.

The next weekly statement disclosed a further reduction in the reserve to 39 per cent., the bullion being £300,000 less, and consequently the rate was raised on 25th June to 4 per cent.

At this time a large loan for the Argentine Government was expected, but it was found impossible to float another issue in the market, and this no doubt hastened the crisis in November.

The increased value for capital here caused a competition for bills by foreign lenders, which had the effect of reducing market rates; the investment of foreign money in bills on London has always been a favourite investment abroad.

In the following week, *viz.*, 10th July, the market rate was equal to the bank quotation. This was due partly to the suspension of specie payments by the National Bank of Uruguay, and it was thought that gold or silver would be shipped to the River Plate.

The rate of discount was raised to 5 per cent. on the 31st of July in consequence of a low reserve in the banking department, but principally due to a crisis in Argentina.

In addition to these facts, we must remember that a large number of new undertakings had been floated by syndicates, and the public not purchasing these new securities a large lock up of capital had followed.

The high bank rate attracted gold to this country in consequence of foreign houses competing for bills, and on the 21st of August the rate was reduced to 4 per cent. Scarcely a month had elapsed before the rate was raised to 5 per cent., and although the gold reserve was low, yet no doubt the Bank directors were guided in their decision by subsequent events, which, however, were not realised until November.

The Stock Exchange settlements showed a large increase, which was due largely to securities being sold to meet losses. For example:—

	1890.	1889.	1888.
	£	£	£
July 1 settlement .	69,059,000	50,762,000	44,825,000
„ 2 „ .	60,970,000	47,525,000	53,009,000
Aug. 1 „ .	53,116,000	53,654,000	46,660,000
„ 2 „ .	59,403,000	48,673,000	45,068,000

The market and bank rates being the same illustrated the scarcity of capital, so that the settlement for the first fortnight in October was concluded with great anxiety.

This settlement foreshadowed the collapse in November, because a great fall in South American securities had taken place. The Bank directors realised the position of affairs, and on 7th November raised the rate to 6 per cent.

Capital became very scarce, and in addition the market was full of rumours respecting the financial position of houses of world-wide repute. When it became known that the great house of Baring was in difficulties, it seemed as if a panic would occur. Fortunately for the credit of this country, the governor of the Bank of England grasped the situation and endeavoured to maintain England's financial position. The leading banks agreed to form a guarantee fund, so that the acceptances of Messrs. Baring, amounting to £15,000,000, would be paid as they matured. The Bank of England also strengthened its position by borrowing £3,000,000 of gold from the Bank of France, and £1,500,000 from the Russian Government. This had the effect of restoring public confidence, and what might have been a great crisis in our commercial history passed away, although the result of the crisis was felt for several years.

It is satisfactory to observe that all the acceptances were paid, and the guarantors in 1895 were relieved of their liability; a company being formed to take over all the outstanding assets of Messrs. Baring.

The Bank also lent freely to those who required accommodation, although 7 and 8 per cent. was charged for such loans. This was shown in the return, other securities having increased to £6,079,000. Such high rates could not but fail to attract capital to this country, and when

this was accomplished the rate was reduced in December to 5 per cent.

The year will always be a remarkable one in the history of finance, because of the new departure by the Bank of England. The large banking institutions of this country are now so important that it is advantageous to seek their aid in order to obtain united action, and thus avert a crisis. Our commerce is so dependent upon credit that it is desirable to afford some protection to *bonâ fide* undertakings at a period when an unsound system of finance might create a panic.

It will be noticed that the question of gold shipments, the rates of interest here and abroad, the position of the Bank of England reserve, the foreign exchanges and the borrowings of our Government are the principal factors to be considered in the money market, and the year which we have considered was no exception to this general rule.

We have endeavoured to show some of the causes which influence the bank rate, and to indicate how the various forces at work in the money market are concentrated, as it were, upon the reserve at the Bank of England. We have also observed that changes in the rate of discount are due to the movements of comparatively small amounts of capital, this being especially the case in the short loan market, where fluctuations occur daily in consequence of the requirements for capital being of a variable nature.

The cause of such changes is of great importance to the banks of this country, since they not only lend their surplus capital in the short loan market, but also regulate charges for loans somewhat in accordance with the official quotation.

The question of cash reserves as affecting the rate of discount is an important one for the banks, and the amount of the contingent fund should, if possible, be as-

certained. If this was thoroughly understood, we might have a less number of changes in the rate of discount, due to the absence or presence of small amounts of gold at the Bank of England. It might also prevent great discrepancies between the market and bank rates, and thus tend to make the latter more effective.

Again, in cases of emergency bullion might be obtained from abroad by the united action of all the banks working for this object in conjunction with the Bank of England.

CHAPTER XIX.

CLEARING HOUSES.

WHEN we consider the old system of banking with that of the present day we find that a great change has taken place. In early times the issue of bank notes was considered the essential part of a banker's business; nearly the whole of his profit was derived from this source. There is, however, a close connection between the issue of bank notes and the growth of deposits in our banking institutions. Any one who had notes in his possession would think it desirable to leave them with a banker for safety, and he thus becomes a depositor; the issue of notes in this country has always preceded deposit banking. We have already remarked that one of the distinctive features of modern banking is that trade is now transacted by means of borrowed capital obtained from banks.

The early bankers issued notes in exchange for the deposits of customers, which were repayable to bearer and on demand. However, in consequence of legislative enactments, it was desirable for the bankers to establish a new method for the withdrawal of money deposited with them. This was accomplished by issuing to each customer a book of order forms, which would enable him to withdraw his capital. As each form was numbered, the banker was able to check the amount of the customer's withdrawals. In course of time this withdrawal form called "check" became altered to "cheque," and is

utilised by all the banks for the purpose of enabling a customer to withdraw his capital.*

Some method was, however, required by which cheques could be exchanged without the use of coin or transmission of bank notes.

In London clerks from various banks were sent out for the purpose of collecting such documents; some of them met in Change Alley, and found it convenient to make an exchange instead of presenting the cheques at their respective banks, the balance being paid in notes and gold.

The originator of the scheme was a Mr. Irving, a clerk to Messrs. Fuller, who suggested that a room should be hired, where clerks from various banks could meet for the purpose of exchange. This was about the year 1775. The ground floor of 7 Lombard Street was then hired for that purpose; but, with an increase of business, the Clearing House was removed in 1814 to No. 2 Lombard Street, the property of Messrs. Smith, Payne & Smiths, a firm of bankers now amalgamated with the Union Bank of London. Such was the origin of the Clearing House, which has been of immense value, not only to banks, but to other similar institutions.

In the year 1839 the average daily transactions amounted to £3,000,000, the balances being then settled by the use of £200,000 in bank notes and a small amount in coin.

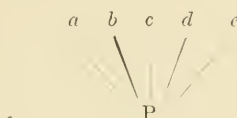
A better system, however, soon came into existence. The banks having found it desirable to keep accounts at the Bank of England, it occurred to them that their differences could be settled by means of cheques drawn

* A cheque is defined by the Bills of Exchange Act, 1882, "as a bill of exchange drawn on a banker payable on demand," but as the laws relating to bills and cheques are somewhat different it would have been better if another definition had been used which at the same time would have preserved the origin of the word.

upon that institution, and thus the use of coin and notes was obviated.

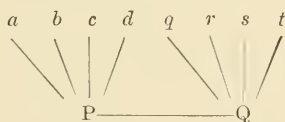
Mr. Jevons * gives the following account of the Clearing House system : “ To obtain a clear view of the way in which bankers help us to avoid the use of money, we must follow up the rise of the system from the simplest case to the complete development of the complex organisation now existing in the United Kingdom ”.

The system of one bank would be as follows :—



Let P represent the banker, and a, b, c, d, e his customers. Payments are made by one customer to the other by simply debiting and crediting. If a owes b money, a 's account is debited and b 's credited.

The system of two banks would be as follows :—



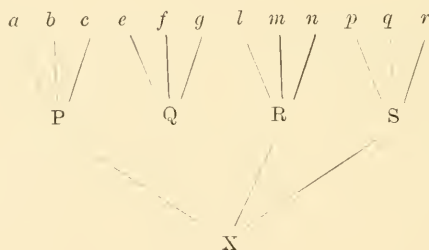
Let P and Q be two bankers in a town, a, b, c, d being customers of P , and q, r, s, t customers of Q . Now, the mutual transactions of a, b, c, d will, as before, be balanced off in the books of P , and similarly with the customers of Q . But if a has to make a payment to q the operation becomes more complex. He draws a cheque upon P and hands it to q . Not wanting coin he carries the cheque to his own banker, Q , and pays it into his account. There will be other persons in the

* *Money and the Mechanism of Exchange.*

town having to make payments in the same manner, and the probability is very great that some of these will result in giving P cheques on Q , and some in giving Q cheques on P . The two bankers will then balance their mutual indebtedness by a single transaction.

In a town with several banks the system is still more complex; such institutions need only to agree to appoint as it were a *bankers' bank* to hold a portion of the cash of each bank, and then the mutual indebtedness may be balanced off just as when a bank acts for individuals.

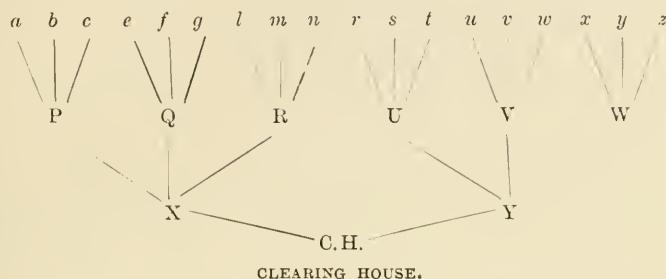
This is the system of the Clearing House. The bankers' bank is the Bank of England, but the accountant's part of the work is carried out at the Clearing House.



Let P , Q , R and S = four banks, each with its own body of customers, and X = the Clearing House. P need not now send a clerk to present bundles of cheques upon Q , R and S , but can pay them into the Clearing House, and by a system of balances their mutual indebtedness can be discharged. The balance is paid by a transfer in the books of the Bank of England.

Only one further step is required to complete the system of connections between each bank in the kingdom and all other banks. Each country bank has a running account with some city bank, and all the city banks daily settle transactions with each other through the Clearing House.

It follows that a payment from any part of the country to any other part can be accomplished through London.



Let *P*, *Q*, *R* be country banks, having the London agent *X*, and *U*, *V*, *W* other country banks, having the London agent *Y*. If *a*, a customer of *P*, wishes to pay *r*, a customer of *U*, he transmits by post a cheque upon his banker, *P*. The receiver, *r*, pays it into his account with *U*, who, having no direct communication with *P*, forwards it to *Y*, who presents it through the Clearing House on *X*, who debits it to *P*, and forwards it by the next post.

This system of country clearing was instituted in 1859, chiefly through the exertions of Sir John Lubbock, now Lord Avebury.

In consequence of its adoption £5,000,000 of gold was not required for currency purposes; the country clearing alone now amounts to about £18,000,000 weekly.

The joint-stock banks were not admitted until the year 1854, but all the metropolitan institutions are not, however, represented at the Clearing House. The Bank of England does not pay its own cheques through the medium of the Clearing House, but it presents all cheques on other banks. The west-end bankers and the various branch establishments in London use the Clearing House indirectly by issuing drafts on a clearing banker.

The Clearing House was, until recently, the property of four private banks; but a company has been formed, and now each bank holds the same number of shares.

There are three daily clearings, *viz.*: 1st, at 10.30 A.M. for bills and country remittances; 2nd, at 12 noon for country cheques; and 3rd, at 2.30 P.M. for bills and cheques.

In 1844 the returns of the Clearing House were equal to forty times the note circulation, but in 1901 they had increased to the proportion of 312.

1844	Proportion of notes to clearing circulation =				40
1868	"	"	"	"	= 87
1869	"	"	"	"	= 90
1870	"	"	"	"	= 97
1871	"	"	"	"	= 113
1872	"	"	"	"	= 135
1901	"	"	"	"	= 312

It is important to recognise the great economy of capital which has been effected by this development of exchange. The use of cheques has to some extent diminished the metallic circulation; similarly the method of transfers between bankers and the establishment of the Clearing House have also economised the use of gold and notes.

The following table shows the increase in the transactions at the Clearing House :—

£
1868 = 3,425,000,000
1870 = 3,914,000,000
1875 = 5,685,000,000
1880 = 5,794,000,000
1885 = 5,511,000,000
1890 = 7,801,000,000
1894 = 6,337,000,000
1901 = 9,561,000,000

The returns for the 4th of the month show to some extent the bill transactions of the country :—

£
1868 = 155,068,000
1870 = 176,137,000
1875 = 245,810,000
1880 = 236,809,000
1885 = 221,873,000
1890 = 289,107,000
1894 = 261,501,000
1901 = 392,279,000

In Edinburgh and Dublin the representatives of each bank meet for the purpose of exchanging their notes, upon the same principle as the London Clearing House.

There are provincial clearing houses established at Birmingham, Bristol, Leeds, Leicester, Liverpool, Manchester, Newcastle-on-Tyne and Sheffield. The amount cleared at such places in 1901 was £603,000,000.

CHAPTER XX.

HISTORY OF BILLS OF EXCHANGE.

THE history of the growth of English industry and commerce reveals to us a series of causes which have materially contributed in building up a highly complex machine, which we designate as the product of industry. Capital (or, in other words, wealth) did not exist in very early times, because then the land was cultivated simply for the purpose of supplying mutual wants. In those days the community satisfied their requirements by means of a system of barter or exchange; however, it was soon discovered that such a system had many inconveniences. The articles to be exchanged did not always satisfy mutual wants, and there also existed the difficulty of defining the ratios or value of each commodity. A medium was therefore necessary which would be accepted as payment for goods bought or sold, besides acting as a standard of value.

It has been already stated that the precious metals, in consequence of their scarcity and other qualities, became at an early period the medium of exchange and a standard of value; and, as people became possessed of wealth, they accumulated the same, because by such means various wants or needs could be satisfied.

A system of hoarding prevailed; gold and silver coins were deposited in strong chests, and represented the capital belonging to the community.

There was scarcely any outlet for the surplus capital of

the country, even so late as the reign of Charles I., and the Church at an earlier period prevented capital from being utilised by declaring it sinful to lend money at usury.

It was not until the people accumulated wealth that a system of credit was established; we have, therefore, first a possession of capital, which found its way in course of time into the storehouse of capital or banks, and then followed a development effected by means of credit documents or bills of exchange. Perhaps, therefore, the most important factors connected with the study of capital are banks and bills of exchange, especially as a means for the payment of goods bought or sold, and also for settling international indebtedness or other great financial operations. We have already seen how the former have contributed towards promoting the material prosperity of this country.

It seems to us somewhat strange that the early bankers, or, as they were then called, goldsmiths, had no dealings in bills of exchange, those instruments of credit being utilised by the Jews for the purposes of money lending; however, in course of time banking and bills of exchange became indissolubly united.

We can scarcely understand how the early bankers transacted business without the medium of bills of exchange, when we consider what is effected in the present day by means of such credit documents. It is worthy of notice that as the method of banking underwent a change, so likewise the use of bills of exchange became somewhat different in character.

For example, the earlier bankers were goldsmiths, who received money for safe custody, and gave in exchange notes which remained in circulation; consequently through the medium of such notes they became possessed of capital which was lent at interest.

It should also be remembered that the system of note issue laid the foundation of our modern cash deposits. We can easily understand how this occurred; the note holder would, in course of time, discover that it was advantageous to deposit the notes which he did not immediately require with the banker, not only for the sake of safety, but also for the purpose of receiving interest on his surplus capital.

The goldsmiths became, in the modern sense of the word, bankers, when they issued notes which would remain in circulation.

In like manner bills have undergone a change in character; the earlier forms were drawn to facilitate the transmission of money from one country to another, but in course of time they were used for other purposes.

The modern trade of this country has been greatly developed by means of credit documents, and as a natural sequence a corresponding increase in the business of banking has taken place.

The early history of bills is of great interest, because we learn that from a remote period a need was felt for something which should take the place of metallic money for the purposes of transmission. Gold and silver coins could only be sent from one place to another at great risk. The Romans recognised the use of bills, and made it legal to sell a debt due from one person to another; if a debt could be sold it was desirable to have some means of transferring it. A written document was therefore necessary in order to transfer debts due, and these documents, known as bills of exchange, were in reality debts owing from one person to another.

Cicero says: "*Sed quæro quod opus illi erit Athenis permutarine possit an ipsi ferendum est*". We have therefore evidence showing that the Romans understood

the utility of bills, and transferred debts by means of them. Bills were used by the Italian and Jewish merchants, and in the fourteenth century they were largely in circulation; in fact, to investigate the early history of bills and of banking institutions we must go to the shores of the Mediterranean.

The utility of banking and bills of exchange was recognised by the Italians long before the system of credit was recognised in this country. The merchants of Genoa, Florence, Venice and other Italian towns sent their ships to the East with goods, and received in exchange gold and silver coins; their surplus wealth was then deposited in the "mounts" or public treasuries, and they received in exchange documents stating the amount deposited.

With the increased trade of the country it was necessary to have credit documents in order to facilitate the payment for goods between the various towns which traded with one another. When bills of exchange came to be used for this purpose, they were the means of extending the operations of banking.

In these Italian towns, banking was of two descriptions, *viz.*, one for money changing, acceptance of deposits and transfer of accounts; the other was of a private character, *viz.*, the lending of money and the discounting of bills. In the former case the municipalities undertook the business of banking, and in the latter the Jews or Lombards were the money lenders.

The use of bills was, therefore, principally in the hands of the Jews, who also found these documents very advantageous when they wished to transfer their capital from one place to another; this was desirable, because they were continually being expelled from various countries. Another incident must not be forgotten which materially increased the circulation of bills, and that was the great

power of the Roman Church. Each country had to contribute tithes to the pope, and these remittances were made either in specie or bills of exchange.

The growth and development of credit documents was also due to a race called the Lombards, who gave the name to a street in London which we might say has become the centre of the financial world. These Lombards were Italian merchants, and were descended from the Longobards, who settled in Italy after the fall of the Roman Empire. They were merchants representing the four republics of Genoa, Lucca, Florence and Venice.

Edward III., in travelling through France, made use of one of the Lombard banks when in need of money, and received from the Bank of the Bardi 5,000 marks, for which he gave an acknowledgment for 7,000 marks.

In course of time these Italian merchants established themselves in London, but at first they did not discount bills, that business being in the hands of the Jews; however, when this race was expelled from London the Lombards became their successors as money lenders. It must be remembered that public opinion had somewhat changed with reference to lending money at usury, because it was no longer considered immoral to receive interest for loans of capital.

The Record Office gives us an interesting example of an early bill. It was drawn 26th September, 1442, by Francesco Venier & Bros., sons of the late Santo, at usance on Obertino de Bardi & Co. in London, and payable to themselves; value received in Venice from Cosmos de Medici & Co., and to be placed to the account of Marino Velliero at the exchange of $44\frac{1}{2}$ per cent. per ducat, the protest being signed by the notary public, Nicolar Acon. by imperial authority, on the 31st December,

1442, Anglican style, *secundum cursum et computationem Ecclesiæ Anglicanæ*.

The above bill is an example of many credit documents which were passing between England and Italy at that period for payment of goods and other purposes.

Bills are said to have been first used in England in the year 1307, and were recognised as a *legal* method of sending money from England to foreign countries (Act 4, Richard II.).

The early history of bills shows us that they were principally used for the purpose of the transmission of money ; they were, however, utilised for the payment of wages or debts due from one person to another. It must be remembered that there were few banks in existence during the seventeenth and eighteenth centuries, banking facilities being then comparatively unknown. The private bankers issued notes, but the amount in circulation was small in proportion to the population ; a want was experienced for some circulating medium, consequently bills were used as bank notes, as well as for the payment of wages.

With regard to the practice of the payment of servants' wages by means of promissory notes, it seems that the system led to abuses, because they were issued for such small amounts as 6d. and 1s., and when unpaid the loss fell upon poor people who could ill afford to lose. This system was happily confined to Yorkshire, but an Act, passed in 1775, prohibited the circulation of promissory notes of less than 20s.

Although the issue of small promissory notes is forbidden, the Bank of France has recently been permitted to discount bills as low as 4s. 2d., and grant loans of £10.

At the beginning of the last century we find bills of exchange largely used for commercial transactions, but such

credit documents were at that time more of the character of bank notes.

Mr. H. Thornton gives a very clear account of the great uses of bills of exchange. He says : “ These documents obviate the necessity of sending gold from one place to another. Let us suppose there are in London ten manufacturers, who sell their articles to ten shopkeepers in York, by whom the said articles are retailed ; and that in York there are ten manufacturers, who sell their goods to ten shopkeepers in London. This trade can be managed by transfers.

“ Letters ordering the transfer of the debt are termed bills of exchange. They are bills by which the debt of one person is exchanged for the debt of another, and the debt, perhaps, which is due in one place for the debt due in another. These bills can be converted into money, or they are discountable. Bills are also accepted as payment, although having some time to run. To possess some article which, so long as it is detained, shall produce a regular interest, which shall be subject to no fluctuation in price, which by the custom of commerce shall pass in certain cases as a payment, and shall likewise be convertible into ready money by the sacrifice of a small discount, is the true policy of the merchant. Liverpool and Manchester effect their business by bills at one or two months drawn on London. The bills annually drawn by the banks of these towns amount to many millions. The banks obtain a small commission on the transaction. Bills are drawn on London from every quarter of the kingdom, and remittances are sent to meet them. While London draws no bills, or next to none, upon the country, London has become the trading metropolis of Europe, and indeed of the whole world.”

We have, therefore, an interesting account of the earlier

methods of banking in connection with bills of exchange, and how these credit documents came into the hands of the private bankers. A hundred years ago travelling in this country was attended with many difficulties; consequently, the transmission of money was somewhat risky. The people found it advantageous to leave their money with the shopkeeper on market days, rather than run the risk of carrying it home. The country shopkeepers occupied an important position in the towns; they drew bills on London, and also sent remittances to this place. Gold occasionally would be paid to their customers in exchange for bills on the Metropolis, which were then remitted with other documents to their London correspondents. Cash was given in exchange for such promissory notes, on payment of a commission for the transaction. Then the shopkeeper painted the word "Bank" over his front door, and engraved the same word upon drafts, by such means bills were circulated in the country. Money was also taken on deposit, and utilised for the purpose of discounting bills.

Thomas Smith, a banker of Nottingham, who had to appear before a Commission of Inquiry in 1711, gave an interesting description of banking business at that period. He says :—

"This Deponent actes in the nature of a Banker, and returnes great sums of money to London, and from thence and diverse other places in this Kingdom, and also for several years past, and his father many years before him, hath used to take in and receive great sums of money of diverse persons, and upon receipt thereof to give notes under his hand for the same, thereby promising to pay the said sum so received to the person authorised in the money or the Bearer of the note upon demand."

In the early part of last century bills were largely used

in Yorkshire for the payment of debts among the small manufacturers and dealers in wool, cattle and corn; they were in amounts of £10 to £30, and were proverbial for their dirty appearance and the large number of endorsements. The most important point in connection with them was that they were very rarely unpaid.

Mr. Leatham in 1841 stated that "bills perform every function that can be assigned to the notes of the Bank of England, with a quality to make remittances by post which the notes cannot possess; and the only specific difference between them is that a limited time is attached to one and not to the other. But when at maturity bills are converted into gold with as much legal certainty as bank notes; when the origin of bills is *bonâ fide* and legitimate, I place them with the security of the drawer, acceptor, and perhaps twenty endorsements on the back, in the first class of our currency, before notes, and next to gold. I know of no purpose of money, except wages, to which bills are not applicable, in the provinces throughout this kingdom, though not seen in London in making payments. It is in the recollection of many persons that all the woollen business of the West Riding was conducted by bills of exchange at two months' date, as low as £5, drawn without stamps, with gold for wages, without the intervention of bank notes, previous to the last war."

We have, therefore, evidence showing that the country bankers in the early part of the present century transacted their business by means of bills of exchange; they also considered that such documents performed the functions of a currency.

Various Committees of the House of Commons, in discussing the position of the Bank of England and the condition of the currency, referred to bills as an important factor in connection with the subject. Thus, in 1810 and

also in 1819 some interesting facts relating to bills were published, and a few years later, in 1832, Mr. Burgess stated that a contraction in the quantity of bank notes in circulation produced directly a much greater relative contraction in the volume of the bill currency. Lord Overstone made the following remarks in 1840 : “ I consider the money of the country to be the foundation, and bills of exchange to be the superstructure raised upon it. I conceive that bills of exchange are an important form of banking operations. Bills of exchange, being an important form of credit, will feel the effect of that contraction in a very powerful degree.”

The evidence thus given tends to show that bills were regarded as forming an integral part of the circulating medium. A great development in the use of credit documents has taken place in recent years, being in consequence of the great growth of English commerce. Now, credit has effected a complete revolution in trade, and has been the means of economising our metallic circulation. The transfer of capital of the country from hand to hand is another illustration of the growth of credit. Greater facilities were required in order to conduct modern trade based upon credit, and this was largely promoted through the formation of joint-stock banks. The surplus capital of the country found its way into these new institutions, and was thus transferred from districts where it was not required to other places where it could be utilised at a profit. The formation of joint-stock banks also increased the use of credit documents ; this is shown from a statement by Mr. Pownall in 1881 as to the number of such documents paid through the London Clearing House :—

LONDON CLEARING BANKS.

Cheques through the Clearing House	71·313 per cent.
Cheques and Bills not cleared	25·248 „
Bank of England notes	2·349 „
Coin	·956 „
Country bank notes	·134 „
	<hr/>
	100·000 „

At the Army and Navy Stores the proportions of credit documents were as follows :—

	1880.	1881.
Cheques	63·67	67 per cent.
Notes	18·6	13·7 „
Coin	17·8	19·3 „

excluding postal orders and notes.

The foreign trade of the country has greatly developed during the present century, partly due to an accumulation of capital, but principally in consequence of the adoption of free trade principles by this country. Goods purchased abroad are paid for by means of bills drawn payable in London.

Commercial dealings, based upon credit, are carried out by means of banks and credit documents; the latter, *viz.*, cheques and bills of exchange, are utilised for the purpose of transferring capital from one person to another.

So great has been the use of such documents in recent years that it was stated by Sir J. Lubbock, now Lord Avebury, that 97 articles out of 100 paid into his bank consisted of cheques and bills. The credit documents which we are now considering, *viz.*, bills of exchange, denote that property is bought and paid for either by the transfer of a debt or a promise to pay later, based upon goods bought or sold. The ability of the banker to lend in reality depends upon the state of trade, and also to some extent upon such credit documents. For example, bills represent a variety of transactions in every depart-

ment of trade, and according to the productiveness of such industries the banker has either more or less to lend. Bills of exchange tell us somewhat as to the condition of trade, and thus we are able to ascertain whether certain industries are prosperous or depressed. For example, if an industry is thriving, we should expect to find in the banker's bill case a large number of bills representing transactions in that particular business; whereas if depressed, a less number of bills would be in circulation.

With regard to the vast number of bills which pass through the banker's hands, it is somewhat difficult to ascertain the purpose or reason why they are drawn. Do they always represent legitimate trade transactions, or are they the result of speculation? On several occasions in the history of banking bills have been drawn against fictitious values.

Merchants accept bills drawn upon them for goods purchased, and incur liabilities on the supposition of being able to discount at their bankers those received; but, if this cannot be done, we can understand how quickly trade becomes demoralised and the industrial machine thrown out of gear.

Our modern trade, conducted through the medium of banks and bills of exchange, reveals to us the fact that credit is very sensitive. For example, credit, or, in other words, capital, may be transferred into bad hands; that is, to persons who do not use it to advantage. Again, by means of credit an unsound business is carried on; fresh liabilities incurred, which, without the medium of credit documents, would cease to exist. We therefore lose in security what we gain in economy by the modern development of finance.

Through the circulation of bills we might say that the whole body of traders becomes, as it were, associated with

the banking community. The ability of the banker to lend is largely dependent upon bills being paid at maturity. Banks and the great instruments of credit, *viz.*, cheques and bills of exchange, transfer the ownership of wealth from one person to another. Bills of exchange, cheques and banks might be compared to machines performing the same kind of work.

London has become not only the financial centre of this country, but also of the whole world. The surplus capital of the country finds its way to London, and from thence is transferred to places where it can be utilised. All the great transactions of the inland trade are, we might say, concentrated in Lombard Street. The country banks send their surplus funds for the purpose of being utilised in discounting trade bills. If such banks require additional capital to meet their requirements, it may be obtained by means of rediscounting these credit documents. London has thus assumed a great financial position; the number of bills drawn upon it exceeds that of other countries.

The Metropolis is, therefore, somewhat like an international Clearing House; our modern system of credit has laid the foundation of a new business, *viz.*, that of bill brokers.

In the early part of the century London had become the centre for all banking transactions. In 1810 Mr. Richardson, who afterwards became a partner in the celebrated firm of Messrs. Overend, Gurney & Co., stated that the nature of an agency of a country bank was (1) to procure money for country bankers on bills when they have occasion to borrow on discount, and (2) to lend the money of the country banks on bills on discount. This system really meant the discount and rediscount of bills of exchange.

At first merchants became agents for the country

bankers, but in course of time the bill transactions were so important that the business assumed a distinct form ; those who carried it on were known as bill brokers. At the same time there was a large increase in the number of country banks which came into existence, partly in consequence of the London bankers, who were anxious to become their agents at a less commission than originally paid to the merchants.

Every new bank which started in the country was the means of increasing the circulation of bills ; such institutions, therefore, considerably developed the use of credit documents. The country banker had, as it were, under his notice the majority of the bills in his neighbourhood. He was thus able to discriminate between good and bad paper, or legitimate trade transactions as distinguished from accommodation bills. First-class bills were discounted by him, and possibly rediscounted in the London market. By this method large transactions were effected between London and the country, consequently there was an increase of business.

The late Mr. Newmarch in 1850 gave an interesting account of the London bill brokers who remitted bills to the country for the purpose of circulation :—

“ B., a banker at Lincoln, has a surplus of £50,000. He is also in the habit of requiring bills of exchange of certain usances and of certain amounts to meet the applications of some of his customers who employ them in the course of their trade. B. might have bills in his own case, but would not reissue, because (1) it would indicate that he was poor, and (2) it would disgust his customers by revealing their transactions to rivals. The London bill broker therefore sends bills, plus the amount of discount due by him on the transaction. These bills had been created in totally different parts of the country, some

being foreign bills. This transaction between London and Lincoln accomplishes four things. The Lincoln bank obtains (1) employment for money; (2) a good security; (3) the bill broker receives £50,000, by which he can discount a further amount; (4) a bill currency is introduced into Lincoln perfectly adapted to its wants.

“ There are three principal modes in which payments of debts are accomplished : (1) The buyer may have no difficulty in placing his account upon the footing of a book debt, where he is debited for what he purchases and credited when he pays; (2) buyer may pay his debts by remitting approved bills; and (3) buyer may undertake to accept bills drawn upon him by the seller. By the first and second modes the circulation of bills is promoted, and by the third mode the *creation* of bills takes place. The bills obtained from London may accomplish seven distinct transfers : (1) Discharges conditionally the claim of drawer or acceptor; (2) discharges claim of payee on drawer; (3) bill broker on payee, supposing the payee to discount the bill; (4) Lincoln banker upon bill broker; (5) farmer upon Lincoln banker; (6) dealer in goods or cattle on Lincoln customer; (7) when sent for payment by dealer’s banker to London correspondent.”

Mr. Newmarch concludes his remarks by stating that “ this skilful redistribution of the bill currency of the country is one of the greatest achievements of our banking system ”.

This method has now become extinct in consequence of the altered conditions of trade; bills are now sent to the country banks solely as investments, and not for currency purposes.

The amount of bills under discount by the banks of the country for the year 1849 was estimated as follows, *viz.* :—

	£
Scotland	15,000,000
Lancashire	12,000,000
England	60,000,000
	<hr/>
	£87,000,000
Foreign	13,000,000
	<hr/>
	£100,000,000
Not discounted	16,000,000
	<hr/>
	£116,000,000

We can quite understand that as the business increased in London in consequence of more bills being sent from the country, it was necessary that merchants who made it their vocation should devote their whole time to the study of these documents; therefore, in course of time, the profession of a bill broker became quite distinct. The vast number of bills which found their way into the London market were exceedingly difficult to understand, since they represented an infinite number of trade transactions. In order to estimate the relative credit of each individual whose name appeared on bills either as drawer, acceptor or endorser, the modern bill broker devoted himself entirely to the study of such documents, which were classified as being either first or second rate. If of the former description, it meant that at maturity they would certainly be paid, but if of the latter class it might be otherwise.

This change in the system of business had some effect upon the banks, because, instead of relying upon the bills held as security, they now depend to a great extent upon the broker; who also receives money on deposit, which is utilised in discounting such documents. However, the position of the bill brokers is one of great delicacy, since they are dependent upon the market for a large portion of their funds. If at times the bankers have no surplus capital to lend, application is made to the Bank of Eng-

land for loans in order to meet such requirements, and this institution is called upon at certain periods to meet large demands upon its reserves.

The London bankers keep a certain portion of their cash with the Bank of England, which has had the effect of making it the final reserve for the country.

The system by which the Bank allows any firm or person respectably introduced to have a discount account is quite different from that of other banking institutions. It seems somewhat of an anomaly that London banks and the Bank of England should supply the bill brokers with funds in order to compete against them; when they are unable to obtain sufficient funds from the former institutions, applications are made to the Bank in order to meet the deficiency in the daily requirements of the money market.

Thus the Bank of England is called upon to meet a large number of demands for loans, which at times amount to a considerable sum. During the commercial crisis of 1857 it lent to bill brokers more than £9,000,000, although advances to the bankers amounted to only £8,000,000; the Bank naturally thought it unreasonable that so large an inroad should be made upon its resources by rival establishments in the money market.

Another important point to be remembered is that bill brokers may carry on their business with a comparatively small capital in proportion to great liabilities.

In recent years the banks, through lending their surplus capital to the brokers, have been the means whereby the latter class has obtained a greater portion of the best mercantile bills; whilst the former discount to a large extent trade bills, such as those drawn by the wholesale houses upon retail dealers in the country. However, the policy in recent years has been to discount bills at

market rates, and brokers will at times offer bills in order to avoid application at the Bank of England. It may happen that the bank rate is, say, 2 per cent., whilst bills are being discounted in the market at $\frac{1}{2}$ per cent. This explains to us the reason why at times the rate is ineffectual to attract gold from abroad. The London banks have lost to some extent what was considered one of the best investments for surplus funds through the modern system of loans to the brokers.

Another point for consideration is whether money lent on demand to bill brokers can in reality be considered as a reserve. For example, if a crisis occurred in the market, and banks called in their loans, it would be impossible to meet such demands without assistance from the Bank of England, which could not possibly entertain all outside applications.

This institution is supposed to find capital at times when the outside market has exhausted its credit, and, being the final reserve for the country, it becomes a very important factor in the money market, therefore its weekly accounts are closely studied.

The Bank's position in the discount market is at the present time somewhat different from what it was some years ago. The large increase in the number of joint-stock banks, holding vast deposits which must be lent, has contributed towards the change. Thus in 1851 the Bank discounted £1 out of every £20 inland bills created, whereas in 1875 there were at least £30 of inland bills created for every £1 of the same discounted by the Bank. In recent years the circulation of such documents has somewhat diminished, in consequence of commercial transactions being on a cash basis. The competition, however, is still very keen between the Bank of England and the various financial institutions.

It has been already observed that the formation of banks and a great development in the use of bills of exchange acted as a stimulus towards increasing the trade of the country. On the other hand, bills have been utilised during periods of speculative activity for the purpose of promoting new undertakings, and thus to some extent have contributed at various epochs in the history of British commerce towards producing a commercial crisis.

We know that the trade of this country is attended with considerable risk; goods are purchased and paid for by means of bills drawn at various dates, but during the interval between the time when the bill is drawn and the day of payment, a series of events may possibly happen. For example, a great fall in price might have occurred in the value of the commodities against which the bills were drawn, or there might be a change in the state of commercial confidence or credit. Traders incur great liabilities; business is transacted upon the understanding that bills may be discounted at *all* times, without reference to other influences which may possibly disturb the money market. If, therefore, one of the links in our modern system of credit becomes broken, the result is sometimes disastrous.

Again, the division of labour has had the effect of making the various industries of the country dependent upon one another; if one is depressed, others are soon affected in a similar manner.

Trade bills represent risks both in time and space: in time when a merchant purchases goods to sell at a higher price at some future date, and in space when goods are purchased to be sold in a distant market. There are, however, less risks in the inland than in the foreign trade. Goods manufactured and sold in this country represent transactions for short periods, whereas in the foreign

trade a longer period elapses between the purchase and the sale of goods; we know also that markets fluctuate considerably, even within a month.

In 1869 74 per cent. of inland bills were for amounts of less than £100, whilst the foreign bills showed only 47 per cent. less than £100, the bulk being from £400 to £4,000.

Commercial transactions are effected by means of such documents, therefore the number in circulation would be a good index as to the condition of English industries. The transactions at the Clearing House on the 4th of each month, which is the principal day on which bills mature, would tell us somewhat whether trade is active or depressed.

The late Mr. B. Price stated * that it is sometimes difficult to ascertain the forces which lie underneath the vast number of bills passing through the bankers' hands. Do they represent legitimate trade transactions or those of a speculative nature?

It is, therefore, important that banks should study closely the credit documents which come into their possession.

Mr. Hankey states that a banker should know the difference between a mortgage and an ordinary bill of exchange. An ordinary bill has such a provision or security; it is based on the transfer of capital in some shape or other in a manner which contemplates that at a fixed date such capital will have passed into the required hands, and that means will be provided to meet it. The other kinds of bills, which we may term mortgages, are based upon money being raised to meet them when they fall due.

* *Currency and Banking.*

CHAPTER XXI.

CLASSIFICATION AND DEVELOPMENT OF BILLS OF EXCHANGE.

THE different classes of bills with which banking is so intimately associated are varied in character.

We have noticed that a great proportion of trade transactions are effected through the medium of credit documents. Goods are purchased and paid for by means of bills drawn at various dates, either by a transfer of a debt due from one person to another, or by a promise to pay at a later date. If a banker looks carefully through the bills passing through his hands, he soon discovers that they represent various transactions.

A primary division of bills would be inland and foreign, the former representing the home trade, and drawn in this country; the latter representing foreign transactions, and therefore drawn abroad, but, as a rule, payable here.

Mr. Newmarch in 1851 classified the inland bills into three divisions, *viz.*: (1) Bills up to £50 of an average amount of £23 8s., with an usance of 2-8 months; (2) bills up to £300 of an average amount of £142 7s., with an usance of 3-5 months; (3) bills above £300, with an usance of 4 months and an average amount of £1,206 3s. The first division would represent retail transactions, and may be described as bills drawn between retailers and consumers. The second class would be that of bills drawn by mercantile firms, although, as a rule,

not in possession of large capital, also of large wholesale houses; in general terms between dealers and retailers. The last division would represent commercial transactions of merchants, producers and manufacturers, wholesale dealers and large consumers of raw material, or, speaking generally, between merchants and dealers.

The number of bills drawn on London from foreign countries is very large; they are the method of discharging international indebtedness, and since the Metropolis has become, we might say, the financial centre of the world, debts are discharged by means of bills drawn upon it.

The foreign bills are for large amounts, being principally in the hands of the bill brokers; they represent to a large extent the proceeds of foreign loans, or payments for interest due to this country. The large number of transactions in foreign bills form an additional element in banking business, which may exercise an important influence at any time.

When we consider the magnitude of these financial operations effected by means of credit documents, and negotiated by the banks of this country, we somewhat marvel at a system of finance by means of which all payments are, as a rule, punctually met.

There has been a large increase in the amount of bills in circulation during the last century; various estimates have been given; the first was made by Mr. Leatham, subsequently Mr. Newmarch, Mr. Palgrave and Mr. Barnett published returns:—

	£	
1832 =	89,000,000	.....
1839 =	132,000,000	.....
1843-6 =	116,000,000	(Mr. Newmarch)
1856 =	180,000,000	Do.
1870-1 =	300,000,000 to 350,000,000	(Mr. Palgrave)
1881 =	1,373,425,920	(Mr. R. W. Barnett)

There would now be some difficulty in estimating the amount in circulation, since the Government returns include stamps for bills, postage and other purposes. The returns of the Clearing House for the fourths of the month give us some idea as to the bill transactions of the country. If all the banks separated the amount of bills held from advances, one would be able to form some opinion as to the amount in circulation.

Mr. John Dun estimated some years ago the amount of bills held, from the returns of those institutions which separated those documents from other advances, *viz.*:—

Scotch banks	.	.	60 per cent. of bills to 40 per cent. of advances.
Irish banks	.	.	69 " " 40 " "
Purely London	.	.	30 " " 70 " "
London and Provincial	50	"	" 50 " "
Purely Provincial	50	"	" 50 " "

There has been a great decrease in the amount of bills in comparison with advances, which is due to commercial transactions being on a cash basis.

The following estimate of bills discounted by the banks was given by Mr. Dun:—

	£
Bills discounted	274,300,000
Less bills rediscounted	30,000,000
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	£244,300,000
Bills held by foreign and Colonial banks, and undiscounted, in private hands	80,000,000
	<hr/>
	£324,300,000
Bills held collaterally against advances and acceptances	20,000,000
	<hr/>
Amount of bills in circulation =	£344,300,000

Mr. Birch, a vice-president of the Institute of Bankers, stated that, from published reports, the bills discounted by the banks are now less than they were nine years ago. He says: "From the published reports it would appear that certain banks (excluding the Bank of England) with

£100,000,000 more of deposits, paid-up capital and reserves than they had nine years ago, have increased their discounts by only £8,000,000, and that the proportion of discounts to the total assets, which in 1880 was 26 per cent., has now fallen to $21\frac{1}{2}$ per cent. The amount of bills taken off the London market by discount daily was estimated by Mr. Palgrave to be £3,000,000."

The number of bills negotiated through banks are so great that it has been found necessary in all the large institutions to have a separate department, so that the work appertaining to such credit documents may be properly conducted.

Bills of exchange are the medium by which the trade of this country is carried on, and when discounted represent the best form of security for money lent. Such documents would be closely examined in order to see whether they are stamped and properly executed. It is necessary to make inquiries as to the standing and position of the various parties, and a record is kept of the information so obtained.

Another class of bills are those left for collection, and designated "short," because of their having only a few days to run; again, these sent for collection by the country banks would form another division, being presented for acceptance if requisite.

We also have bills drawn by country banks upon London institutions, and it is necessary that such documents should be accepted. There are also foreign bills sent to London for sale in the market, at the current rate of exchange.

Again, we have bills drawn abroad by foreign correspondents on their London agents, and known as acceptances in the market; they are so important in the present system of banking that it is desirable to show how they differ from ordinary mercantile transactions. Some of the

bills drawn abroad by foreign correspondents are utilised for the purpose of making a profit on the variations in the exchanges upon England.

There are also a large number of such documents payable in the country, which the London bank is called upon to collect; this is done by remitting the same to various country banks.

In consequence of advances to bill brokers, a large number of bills which have been discounted are left as security for the due repayment of the loan; capital so lent is designated as "money at call".

The bill brokers discount bills payable in the country if drawn on first-class firms, which require collection at maturity. It is manifest that great care and attention is required in dealing with these credit documents. The stamps are first examined in order to ascertain whether the duty is correct, and then if the endorsements are in order. The next step is to obtain acceptance, if necessary, and finally the due date is carefully marked upon them. It is very important that they should be presented for payment at maturity, because if not paid they must be either noted or protested for non-payment.

Another important class would be those conditionally accepted being paid on production of bills of lading and shipping documents. For example, a consignment of cotton is made to this country; the bills of lading are forwarded together with bills of exchange, and when acceptance has been obtained the shipping documents are delivered. Such bills form an important class of security, and some knowledge respecting them is desirable.

When a bank receives such documents as security it is necessary to note the due date of the vessel by which the

goods are shipped, in order to get possession of the dock warrants which represent the same.

When an importer wishes to obtain the goods which are represented by the bills of lading and other shipping documents, he must get possession of the bill of exchange; in order to do this he has to pay rebate, *viz.*, interest from the time it is taken up to the date of maturity. The London banks allow this on payment of $\frac{1}{2}$ per cent. above the deposit rate.

We can see that it is important for the importer to get possession of these documents when the goods are perishable, or when a sale can be effected at a good profit, because a fall in prices might occur if not sold at once.

Commercial transactions throughout the world are represented by bills, and negotiated daily in every large banking institution. The small number which are unpaid at maturity is an illustration of the safety of such documents, either for the payment of debts or as bankers' security.

We have considered bills in their commercial character and it is now desirable to regard them in their legal aspect. As bills were utilised in the payment of debts from an early period, it was necessary that they should be in every sense transferable; consequently by the law merchant they became documents of perfect negotiability.

It has been noticed that bills were a legal method by which money could be sent from London to foreign countries in the reign of Richard II. Subsequently, to 1770 bills of small amounts circulated as bank notes, in consequence of an absence of banking facilities in the country. Bills of less than 20s. were in circulation, and were utilised for the payment of wages. However, it was found that many of these small bills were unpaid, and the loss fell

upon the poorer classes; consequently the Act of 1775 prohibited their use.

Mr. Chitty states that bills and promissory notes were not assessed with stamp duty in England before 1782, when the special exemption of 5 Will. and Mary, cap. 21, sec. 5, was repealed by the Act 22 George III., cap. 33, and scales of duty were imposed; but subsequent Acts of Parliament increased the duties payable on the issue of bills.

The most important Act relative to bills is that of 1881, which codified the existing law relating to credit documents. Mr. Judge Chalmers, the author of this valuable Act, states that the law is founded upon a series of judicial decisions which were determined by the customs of trade.

The great bulk of the law relating to negotiable instruments is contained in the reported cases, which are very numerous; the last edition of Byles on bills cites more than 3,000 cases on the subject. Contrary to the general rule in the law of England, the benefit of a contract arising on a bill of exchange is assignable, and consideration will be presumed unless the contrary appear.

We have seen that they were used in England so early as the reign of Richard II., but the first recorded decision does not occur until the time of James I.

The courts for a long time regarded bills with jealousy as an exception to the common law, and restricted their use to merchants, but at last their obvious utility overcame the scruples of the judges. A bill of exchange is defined by the Act of 1881 to be "an unconditional order in writing addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay on demand, or at a determinable future time, a sum certain in money to, or to the order of a specified person, or to bearer". Every endorsement on a

bill really constitutes the endorser as a new drawer, and the endorsement admits the signature and capacity of every prior party, so that every endorsement on a bill is to a banker an additional security, unless it is forged, which would have the effect of cancelling subsequent endorsements.

The usual form of a bill of exchange is as follows :—

£200.

LONDON, 1st January, 1897.

On Demand (or at sight, or at months after date) pay to my order the sum of Two Hundred Pounds value received.

JOHN SMITH.

To Messrs. BROWN & JONES,
Sheffield.

The following are some of the principal provisions with regard to bills of exchange :—

Such documents require an *ad valorem* stamp, and if not otherwise stated three days of “ grace ” are added to the time of payment.

A bill is “ negotiated ” when it is transferred from one person to another, so as to constitute the transferee the holder of the bill.

If a bill is to bearer it is negotiated by *delivery* ; but if to order by the endorsement of the holder, completed by delivery.

A bill must be presented for payment by the holder on the day it falls due, or else the drawer and endorsers will be discharged.

In connection with a bill of exchange we have the drawer, the acceptor and the payee. The payee may be a fictitious person without invalidating the bill (section 10, 7, (1)), and the bill may be treated as payable to bearer.

A bill of exchange is an unconditional order to pay a certain sum of money addressed by one person to another who must be named. This sum of money is payable on demand, or at a fixed or determinable time, such as at a

fixed period after date or sight, or after the occurrence of a specified event which is certain to happen.

If a bill is not payable to bearer the payee must be named or otherwise indicated with reasonable certainty.

If it does not contain words prohibiting transfer, it is payable to the person named or to his order at his option.

A bill is payable to bearer which is expressed to be so payable, or on which the only last endorsement is an endorsement in blank.

A bill is dishonoured by non-payment when it is duly presented for payment and payment is refused or cannot be obtained, or when presentment is excused and the bill is overdue and unpaid.

A bill is discharged by payment in due course by or on behalf of the drawer or acceptor.

The custom of making bills payable at a bank is comparatively modern, and a holder could object to receive a bill so accepted.

Of course, it is a great convenience for traders to make their bills payable at a bank, but unless there is a special agreement between the banker and his customer it is doubtful if the latter could make any claim against the former in case of refusal to pay bills. A banker is compelled to pay cheques, providing he has funds belonging to his customer, but a bill of exchange is outside the relation of a banker to his customer.

It might be desirable to consider whether banks should undertake any risk in the payment of bills for their customers, when they are held liable for forged endorsements. It is impossible to verify endorsements, therefore the law relating to bills ought to be assimilated with that of cheques, in order that the banker may be protected in case a bill is so paid.

The French code indemnifies a bank for paying bills,

although possibly the endorsements may not be in order.

Some protection may be obtained against losses if bills were only paid in cash to another banker.

It is not an uncommon procedure in London for bills to be presented for payment and bank notes obtained in exchange, in order to wire the fate of such documents.

An additional protection may be obtained if the banks insisted that bills should only be paid with cheques attached; of course, safeguards such as these are not beneficial to the trading community; therefore, if the law could be amended no change in the present method of payment would be requisite.

As bills also form the means of settling international indebtedness, it would be advantageous if the law, with regard to those instruments, was identical throughout the world; in France a bill represents a trade transaction, and therefore it does not circulate; it must state on its face that value is received in goods, value received in cash or value in account. In this country the law raises a *prima facie* presumption that value has been received.

It was discussed at a meeting of the Institute of Bankers in December, 1879, whether certain changes relative to bills should not be made. The abolition of days of grace was considered desirable, now that the means of communication are so rapid, and this has been done in the United States. It was, however, thought necessary to retain conditional acceptances, which are bills payable on the delivery of bills of lading and shipping documents, and as they meet the requirements of the foreign trade of this country are beneficial. The question was also raised whether it would be desirable to impose restrictions upon the issue and circulation of accommodation paper.

With regard to accommodation paper it was not con-

sidered desirable to restrict the issue and circulation of bills which might appear irregular, although possibly they may not represent trade transactions. The French and other foreign codes state that such credit documents are illegal.

It is important that the position and liability of each party to a bill should be known, so that, if necessary, the right persons may be sued on non-acceptance or non-payment.

When an inland bill is unpaid, it is customary to have the same noted ; but a foreign bill should always be noted and protested, although in the present day the noting of inland bills is not considered in all cases necessary.

Our modern system of credit has been the means of utilising bills in order to obtain loans from banking institutions. This is effected by means of drafts which are, as a rule, drawn by foreign correspondents, who deposit securities to cover the advances so obtained. Such documents are known as acceptances, which are readily discounted by the bill brokers, and designated "bank acceptances" in the money market.

Mr. Dun has subdivided acceptances into the following classes :—

1. Drafts of seven, fourteen or twenty-one days, drawn by country bankers for the purposes of remittance.
2. Acceptances up to ninety days against credits established by banking correspondents in the country.
3. Acceptances on account of foreign and colonial banks having head offices in London.
4. Acceptances to mercantile firms and companies abroad.

With regard to the third class, they ought to be kept within bounds, and the last division should be avoided altogether.

With regard to such credit documents there is always

an element of danger, especially when a feeling of distrust exists in the mercantile world.

A bank which is perfectly solvent may have accepted a large number of bills against which it holds sufficient cover. When, however, a crisis occurs, such bills may be refused in the market, especially if there are a large number offered for discount. If this occurs the bank's credit would be materially injured, and, as a natural consequence, may possibly lead to its failure.

One of the noticeable facts in connection with the City of Glasgow Bank's failure was that within a week after its acceptances had been refused in the market the suspension occurred.

Another risk with regard to acceptances is that many changes may occur between the interval of acceptance and the day of payment.

The chairman of the London and Westminster Bank stated some time ago that "acceptances drawn by mercantile firms abroad is part of the business that ought to be carried on by a merchant or merchant-banker".

It has been represented by those who are in favour of acceptances that if the business is kept within bounds it is perfectly safe, and banking institutions which have transacted such business have made few losses. Of course, it is important that acceptances should be fully covered by means of the deposit of first-class securities as a protection against any loss that might arise.

Acceptances are sometimes utilised in Stock Exchange transactions, securities which are bought being deposited as cover, but this kind of business would certainly be discouraged.

The acceptances of six of the principal London banks show a considerable decrease from 1880 to 1888, *viz.*:—

£

1880 = 9,470,000

1888 = 7,153,000

In 1901 the acceptances of the joint-stock banks in England and Wales were £16,000,000.

In consequence of various banking amalgamations it is not possible to give the amounts of the above-mentioned banks, but the acceptances of ten London joint-stock institutions in 1903 amounted to £9,712,000, against deposits of nearly £230,000,000.

At the present time there seems to be a decrease in the amount of bills in circulation, which is partly due to the fact that modern trade is based principally upon cash transactions; many firms dealing with wholesale houses find it advantageous to pay cash for goods purchased rather than give a three months' bill; the trader then gets the benefit of the discount allowed by the wholesale firm on such transactions.

The great increase in the business of co-operative stores, where all sales are for cash, has also been the means of lessening the number of bills. Formerly the trade transactions of such stores were in the hands of shopkeepers who sold goods on the credit system, and therefore were not able to pay cash for goods bought; consequently the retail dealer was at times compelled to give bills to the wholesale manufacturer. It has been stated that during the busy season at a London co-operative store the daily receipts amounted to £10,000.

Again, the means of communication are now so rapid that it has materially assisted the present system of cash payments; country cheques form the mode of payment instead of bills. Cash can be obtained for these cheques through the medium of the Clearing House in the course of a few days.

The Clearing House statistics show a decrease in the amount of bills payable on the fourths of the month from 1874 to 1886, but since that date there has been a considerable increase.

CLEARING HOUSE RETURNS, 4TH OF THE MONTH.

	£
1875 =	245,800,000
1880 =	236,809,000
1885 =	221,870,000
1890 =	289,107,000
1895 =	283,610,000
1900 =	372,460,000

PROPORTION OF 4THS TO TOTAL AMOUNT OF CLEARING.

1877 =	4·6 per cent.
1892 =	4·0 „
1901 =	4·1 „

There has been a large increase in the use of country cheques; according to the Clearing House returns the amounts were :—

	£
1884 =	443,000,000
1885 =	426,000,000
1889 =	522,000,000
1902 =	884,869,000

In 1903 the weekly amount was about £18,000,000, so that would give a yearly total of £936,000,000.

In 1880 Messrs. Glyn, Mills, Currie & Co. cleared 19,950 cheques in one day, of which $2\frac{1}{2}$ per cent. were under £1; but in 1887 they cleared 35,090, of which 4 per cent. were under £1.

Whilst, therefore, bills have decreased, there has been a large increase in the cheque circulation of the country; the system of telegraphic transfers has also contributed largely towards decreasing the number of bills drawn.

Mr. Birch gives an interesting account showing how these transfers act as substitutes for bills. “ Formerly the

banks and great commercial houses in the East, in the United States and elsewhere took, as they do now, the ordinary trade bills, *i.e.*, drafts against documents of consignments and such like, at six, four, three and two months at the ordinary usance, and any one requiring first-class clean bills for remittance, either for the purchase of commodities, or to cover credits or other purposes, would apply to these banking institutions, who would give bills also at usance. Thus, there were running two sets of bills representing one commercial transaction. Now, these banking institutions continue to take these trade bills as formerly, but, instead of drawing at usance, they give telegraphic transfers, which enables a merchant in Hong Kong or in New York, or in any other part of the world, to calculate exactly the cost of his operation, just as if he were sitting in London ; no question of discount, of bill stamp or other expense, or whether the bill be a good one. He can balance his operation just as well at these distant places as if he were sitting in Lombard Street."

Bills are utilised in the present day in the manufacturing towns of the North of England for the purpose of settling trade transactions. Thus the monthly settlements at Bradford, Huddersfield and Leeds are effected by means of drafts drawn upon London.

We have already noticed that the largest proportion of bills in circulation is in the hands of the bill brokers, which is certainly one of the features of our modern system of finance. The large increase of business on the Stock Exchange has no doubt somewhat increased the number of bills in circulation ; however, there are a less number of inland bills, although foreign bills are increasing. The latter are utilised for the purpose of withdrawing capital obtained in this country for investment abroad.

Again, the payments of interest by foreign countries are made by means of bills of exchange. These payments are very large. For example :—

			£
Jan., 1903	Dividends	. . .	3,826,000
	Drawings	. . .	205,000

It will therefore be seen that although there has been an increase in certain classes of bills, yet, collectively, there has been a decrease; this has somewhat affected the business of the notaries, who in former days were fully occupied in noting and protesting such documents.

It is certainly a cause for regret that the banks do not discount so many bills as formerly, because such credit documents are justly considered as one of the best investments for surplus funds. Mr. Hankey says that bills of exchange are the only kind of investments upon which absolute dependence can be placed for a return of capital at a fixed date.

Good commercial bills of short dates have an advantage over Government stock or Exchequer Bills, because the banker is certain to receive back the same amount of money which he advanced; whereas there might be a depreciation in the value of stock.

The large amount of bills held by banks as security against advances to bill brokers is evidence of the fact that they are considered as a first-class investment.

Again, bills can be utilised for the purpose of rediscount in cases of emergency or other reasons; some country banks prefer keeping their reserves in bills rather than in Government stocks; from a banker's point of view a decline in the circulation of bills is to be regretted.

In consequence of a decrease in such documents the loans to the Stock Exchange show an increase, but it is questionable whether this is a change for the better. From the

published reports of certain banks, we find that advances, which are largely made up of such loans on the Stock Exchange, have increased by £52,000,000, and the proportion to the total assets has risen from 34 per cent. to $38\frac{1}{2}$ per cent.

In order that we should be able to form some idea of the amount of banking transactions in such documents it would be necessary to separate bills discounted from advances in the half-yearly statements which are issued to the shareholders.

In conclusion we may state that bills have largely contributed towards promoting the growth of English commerce, and thus been the means of placing our credit in the highest position throughout the civilised world. This, however, could not have been attained without the use of banking institutions; consequently they have also shared in the prosperity of the country through the circulation and use of such credit documents.

CHAPTER XXII.

BRANCH BANKING.

ONE of the distinctive features of modern banking is the establishment of branches throughout the country, and the result has been twofold, *viz.*, a large increase in deposits and a diminution in the paper circulation of the country. No doubt a great number of persons who formerly did not keep a banking account have availed themselves of the privileges which the branch banks now give to customers.

The following table shows the increase in banking offices :—

	Offices.
1858	2008
1872	2924
1883	3932
1891	4934
1899	6367
1902	6672

The branch system is carried out more extensively in Scotland than in England or Ireland, if we compare the number in proportion to the inhabitants.

The present number of branches are :—

England	4895
Scotland	1087
Ireland	690

Although branches may be of great service to the community, it is advisable, however, to consider them from a banker's point of view.

Mr. Rae, in his excellent book, *The Country Banker*, has stated that a branch should not be opened unless, possibly, for the following reasons :—

1st. It should be advantageous for the customers of that bank.

2nd. There should be a possibility of new business being obtained.

3rd. That the branch may act as a connecting link to other branches.

They should not, however, be opened simply for the purpose of competing with a rival establishment.

It must be remembered that when a bank is opened there is always the tendency for the new institution to get the bad or doubtful accounts of the district.

Branch banks are, no doubt, of great service in providing an outlet for surplus capital; for example, if it cannot be employed with advantage in one district, there might exist a demand in another, so that all the resources of the banks are utilised. If the surplus funds of a bank can always be lent at a profit, it follows that a higher rate of interest could be given for deposits, or larger dividends paid to shareholders.

The late Mr. Gilbert, in his treatise on banking, says that for small towns a branch of a large bank is more advantageous than an independent establishment, since the former can be worked at less cost.

The recent amalgamations of banks would, however, prevent new institutions from starting, because the resources of the head office would be much larger than a small local bank; competition, which is generally advantageous for the community, is not required in the case of banking.

In Scotland the branch system has been so extended that it is almost impossible to form a new bank; the Scotch

banks have also the privilege of issuing notes, which enables them to provide till money at a trifling expense.

Competition between banks is not desirable, since greater risks and responsibilities are sometimes undertaken in order to secure profits.

Of course, it is requisite that banking facilities should be provided at a small cost, but such advantages should not be at the expense of stability; if a branch can be opened, the small trader and shopkeeper is enabled to keep banking accounts.

The large increase in the country clearing in London shows that the branch system has been the means of inducing a fresh class of people to open banking accounts.

Mr. Barnett in 1881 estimated the country clearing at £350,000,000 per annum, and since that time there has been, as already stated, an enormous increase in the amount passed through the Clearing House. This shows that the branches have obtained quite a new connection; they have also been the means to some extent of superseding the country note circulation, since cheques are now more utilised. These documents, which are received at the branches, can be transmitted to London daily, where they are liquidated through the medium of the Clearing House.

Some years ago a bank with branches could get a London agent to transact its business at a lower cost than a group of small banks which collectively paid more commission. This advantage is, however, not so important in the present day, because of recent amalgamations of banks with London offices. It is, however, essential for a bank to open branches in order to increase its connection, when by such means the new business obtained represents various industries, so that a depression of trade would not then be so severely felt. In such a case they

act as feeders, and give, as it were, new life to the central establishment. Again, if customers have greater facilities offered them, it is natural to suppose that they would recommend the institution to their friends.

The branch system also implies greater facilities for the transmission of money from one district to another.

Of course, the opening of new offices should increase the dividends to the shareholders, since banks naturally wish to increase their profits, if it can be done with safety. It seems, however, that the additional facilities have to some extent benefited the customers rather than the banks.

The following figures show dividends paid and number of branches after various intervals of the following banks :—

Bank.	1885.		1891.		1903.	
	No. of Branches.	Dividend.	No. of Branches.	Dividend.	No. of Branches.	Dividend.
		Per Cent.		Per Cent.		Per Cent.
Alliance	5	7	12	8	158	20
Capital and Counties . .	59	18	132	18	350	18
Central	7	10	11	10	439	18½
City	8	10	12	11	...	...
Consolidated	4	10	9	10	...	...
Imperial	4	7	7	7	...	...
London and County . .	160	20	173	22	225	22
London Joint-Stock . .	6	12½	10	12½	39	12
London and Provincial .	84	12½	119	15	224	18
London and Westminster .	9	16	15	16	35	14½
National	110	11	103	10	114	11
National Provincial . .	153	20	167	20	281	19
Union of London & Smiths	5	12½	9	12½	104	12
London and South-Western	53	6	91	8	147	16

The above-mentioned fourteen banks have been reduced to eleven by amalgamation. The Alliance and Consolidated form part of a group known as Parr's Bank; the Central and City have amalgamated with another series known as the London City and Midland Bank; and the

Imperial Bank has been merged into the London Joint-Stock Bank.

We notice that banks which have increased their dividends are, with few exceptions, those which have opened branches in places where no banking accommodation previously existed; for example, the London and County, London and South-Western and London and Provincial have opened branches in districts of greater London, where no bank had hitherto been established. Although deposits have largely increased there has not been a corresponding increase in dividends, which shows that the depositor has benefited by means of additional banking facilities. We must not, however, forget that in recent years there has been a steady decline in the rate of interest ruling in the market.

These banks, however, have considerably increased their reserve funds, which is very satisfactory, because it shows that they have provided additional funds to meet sudden emergencies.

Again, the additional reserve takes the place of augmented capital, which is necessary when we consider that the liabilities have increased £10,000,000. Although some of the provincial banks have opened additional branches, yet their dividends do not show a corresponding increase. For example :—

Bank.	1881.		1891.		1903.	
	Branches.	Dividend.	Branches.	Dividend.	Branches.	Dividend.
		Per Cent.		Per Cent.		Per Cent.
Wilts and Dorset . . .	64	22	83	22	94	21
Manchester and Liverpool	54	20	50	20	54	20
North and South Wales .	50	17½	65	15	75	16
*Lloyd's Bank . . .	43	20	130	17½	406	17½

* Now a London institution.

However, if the opening of branches has prevented other new banking institutions from starting, the result may in course of time be favourable to the existing establishments.

We will now consider some of the disadvantages which arise under the existing system of branch banking. It has been alleged that each office is in some sense a source of weakness, and this we believe is the reason why the Bank of England has not adopted the modern system of banking.

A recent writer in the *Economist* suggested that the Bank of England should have a large number of branches, like the Imperial Bank of Germany, which has at present 250, but we must not forget that the former institution holds the cash reserve of this country. The existing banks would not for many reasons like to see the Bank of England as a competitor. The establishment of a branch means an additional responsibility to the directors, who are somewhat unable to understand thoroughly all the details, and have a practical insight into the business of a town far away from the head office; they must, to a great extent, be guided by the manager who supplies them with the necessary information. However, the *real* responsibility for every branch institution must rest with the directors, who, however, rely upon an efficient system of inspection, which is the essence of the present method of banking.

Lord Goschen, in his celebrated speech at Leeds on 28th January, 1891, mentioned that eleven large banks kept in cash only 10·3 per cent. in 1888, whilst in 1879 they held 12·9 per cent. There does not appear to be any connection between the amount of cash held and the number of branches; the monthly returns issued by some of the banks show that banks with the largest number have occasionally a small cash reserve. No doubt if each branch

was a separate institution, a larger cash reserve would be held. On the other hand, one must not forget that facilities for the transmission of coin and bank notes are greater now than they were fifty years ago.

It is also possible that an issue of £1 notes, as advocated by Lord Goschen, would be distinctly advantageous to a bank with a large number of branches. These notes could be sent to any branch at a trifling expense compared with the cost of transmitting gold.

There does not appear to be any fixed rule as to the amount of cash which a bank should keep in reserve. The ratio per cent. of cash to deposits and acceptances varies from 12 per cent. to 21 per cent. in the case of London joint-stock banks; the National banks in America keep \$1 in cash for every \$4 deposited, which gives a proportion of 25 per cent., and it may be noted that branch banking in America is discouraged.

We know that banks succeed because great confidence is placed in them, but if a branch establishment lost a considerable amount of capital it might cause a run upon all the others. An institution may be perfectly solvent and yet obliged to close its doors, in consequence of the head office being unable to supply notes and gold to a large number of branches with sufficient rapidity.

A bank with a comparatively small number of branches may be in some respects relatively stronger than one with a large number. The former would have, as it were, its business more concentrated, and consequently be able to supervise it more thoroughly. If a bank opens additional offices the capital should possibly be increased. In the United States no new bank is allowed to be formed unless a certain amount of capital is assigned; the weakness of our system is an increase of liabilities without a corresponding increase of capital. In recent years the banks

have seen the danger, and have made considerable additions to the capital and reserve funds.

Mr. Gilbert stated some years ago that a bank's capital should not be less than one-third of its liabilities ; no doubt this is a very high proportion, but it is questionable whether 10 per cent. is sufficient.

If we study the balance sheets of the Scotch banks we find that, although their deposits and branches have increased, their capital accounts remain practically stationary. Thus :—

	Capital. £	Deposits. £
1865	9,431,000	56,185,000
1875	8,785,000	78,405,000
1881	9,052,000	78,283,000
1891	9,052,000	92,887,000
1900	9,302,000	103,674,000

It must also be remembered that the Scotch banks have accepted the responsibilities of London institutions, but their reserve funds have been increased to some extent. Quite recently in Scotland it was found necessary to reduce the rate of interest on deposits, because of the difficulty experienced in the employment of surplus funds ; but, on the other hand, the rate of discount has been correspondingly lowered. The English banks have also increased their capital and reserve ; for the year ending June, 1902, there was an increase of £269,000.

The capital of ten London banks amounts to £18,000,000, against deposits amounting to £230,000,000.

Another disadvantage of branch banking has been the tendency in recent years to open branches in places where rival establishments exist. Possibly at such places there was enough business for one bank, but, with another competitor, the profits would be reduced to a minimum.

There is no doubt that the opening of branches has been

the means of extending banking facilities to a class who formerly did not avail themselves of the privilege. We might say that fifty years ago no one opened an account unless a large balance was kept : in those days banking existed principally for the wealthy. At the present time, however, any person may have a banking account, provided a small commission is paid.

The large increase in the deposits of the banks must be principally due to the fact that a new class have availed themselves of such privileges.

We have already mentioned that the enormous increase in the country clearing in London is partly due to the increased banking facilities offered by the existing banks.

The following table shows the increase in the number of banking offices in various large towns, and we presume that branches would not remain open unless a profit was made :—

PROPORTION OF BANKS TO NUMBER OF INHABITANTS.

	1872.	1886.	1901.
Birmingham . . .	31,000	15,000	9,325
Bradford . . .	...	15,000	15,540
Leeds . . .	25,000	28,000	10,462
Liverpool . . .	29,000	12,000	8,352
Manchester . . .	18,000	9,000	5,281
Sheffield . . .	...	47,000	12,690

Between 1877 and 1901 banks were opened in 1,108 places where no bank had previously existed, and these facilities for banking have been of much value to the community.

However, we must consider whether the present banking system is advantageous to all classes of society ; the tendency of modern banking is one of amalgamation. Banks are not being formed for the purpose of providing additional facilities, which from time to time are

necessary on account of growth of population and increased commerce. No doubt the public may benefit by these amalgamations in one way, *viz.*, by reducing the cost for banking accommodation; the working expenses of two amalgamated institutions ought to be less, especially if competition had previously existed between them.

On the other hand, it is not desirable to establish a monopoly of banking; we know that in Scotland it would be impossible for a new bank to start with any prospect of success. The branch system has been so extended, combined with a monopoly of note issue, the *sine quâ non* of Scotch banking, that it would prevent a new institution from making a profit. It is possible that if the £106,000,000 of capital deposited in the Scotch banks were divided amongst twenty banks instead of ten, there would not have been the necessity for London offices.

A system of monopoly might be the means of increasing the charges for banking facilities; therefore it is desirable to consider whether there is any probability of its being established in this country.

There is one defect in the branch system which is not advantageous, *viz.*, the continual reference to the head office on all business of importance in connection with the branch. We believe that in some banks no loans above a certain amount are allowed, unless sanctioned by the central establishment; this not only means delay, but it also makes the board of directors practically responsible for the business of every branch.

Again, it is somewhat difficult for the directors to judge accurately upon a written report what is the real position of their customers. A *bonâ fide* applicant might not be able to get the accommodation he requires; we know that capital may be lent in some cases to persons without any risk—in fact, without security—if a personal knowledge

is obtainable ; a board of directors cannot possibly judge of those who are practically unknown to them.

A bank may be transacting business in 150 different places, where a diversity of trades and manufactures exists ; whether the branch system is a perfect one for the community at large is a matter for inquiry.

Some banks have recently appointed local directors in order to look after the requirements of particular districts.

A writer in the *Economist* stated that the centralisation of control means the stifling of individual intelligence and energy, coupled with failure to gauge the needs of local commerce. It also meant the starving of enterprise in the provinces, because the capital of each district was sent to London for investment. No doubt a local institution was more inclined to assist new undertakings than a London board of directors. Of course, it is possible for a branch manager to state accurately the requirements of the district to the head office, and thus satisfy local requirements. Possibly local banks with few branches, say for every county of England, or spread over certain defined areas, would have been preferable, but the recent amalgamations tend to show the desire for a London office.

If a bank with a large number of branches failed, the distress occasioned would be felt over a much larger area than if confined to one district. There is, of course, less possibility of capital lying idle in the case of a bank with branches over a large space, because, if not required in one district, it may be utilised in another. Banking, however, is now so much centralised in London that the Metropolis has become the great distributor of capital. What we really want in banking is economy, combined with efficiency : our system must not only supply the wants of the community, but it must be also perfectly sound. No feeling of distrust should exist with regard to

our institutions ; every one admires and has an unlimited faith in the Bank of England, because strength rather than dividends has been the policy of the directors ; it might have had branches throughout the country, but did not care to extend its responsibility, whilst holding, as it were, the key of our banking system. We presume the Bank recognised the fact that new branches established meant, in some degree, additional responsibility and weakness, as well as another outlet for specie payments.

We have already noticed that, with few exceptions, dividends have not increased by the establishment of branches ; on the other hand, it is thought that banks which pay high dividends should give cheaper and better facilities to the public. It might, however, be stated that the increased facilities given by the banks are really cheap, when we consider that reserve funds of £29,000,000 are held, upon which the shareholders receive no dividends. However, competition and the tendency for the rate of interest to decline are really the causes of stationary dividends. The profits made by banks on their total resources seem small ; for example, some years ago it was shown from returns that the purely London banks only earned 10s. 10d. per cent. on their total resources, although the proportion for country banks, who charge higher rates for loans, was from 15s. to 19s. 8d. per cent. Competition between banks is not desirable if it results in speculation in order to maintain dividends ; on the other hand, it is of vital interest to the community that we should not have a banking monopoly.

Mr. J. B. Martin stated in the *Economic Journal*, on "The Evolution of our Banking System," that "the provincial banks under the old system have done good service to the trade of this country. Intimately connected with the needs of their district, the position and character

of their customers, they have fostered and developed local trade, agriculture and industries in a manner that might be impossible under new conditions. It has been made a complaint from Scotland that the resources of the country have, since the Scotch banks opened branches in London, been diverted from their legitimate use to the Metropolis, and that heavy discount rates are charged locally, while the money is being employed at lower rates in the London money market. The same complaint has here and there been made in England, and it seems desirable that any change in the conditions of banking in this respect should take place gradually, rather than by any sudden movement that might entail some dislocation of local trade and industry."

In connection with this subject we might observe that a bank which has gradually increased its deposit is somewhat different to one whose business has been obtained through a series of amalgamations.

Some years ago it was stated by the official liquidator that one of the reasons why a certain institution failed was the difficulty of obtaining effective control and proper supervision over branches so far away from the central establishment.

We have stated some of the objections against the formation of large banks in this country, but as this has already been accomplished, it is necessary to see how the new system of banking can be strengthened. The most important safeguard is an effective system of audit, carried out by inspectors, who can make a thorough report as to the business of each branch.

The weekly reports sent should contain every particular of importance with respect to new accounts, the amount advanced during the week, and also what bills have been

discounted. Any important fact which had transpired should be communicated by the branch manager.

The quarterly reports should review all the important events in the history of the branch, with a detailed account of the loans effected during that period.

The half-yearly report is more in the nature of a balance sheet, since it gives particulars as to profits made, such amount being transferred to the head office.

There must be also a continual check on the cash and securities held at each office. It is also of importance that a sufficient cash reserve should be held; Mr. J. H. Tritton, the President of the Institute of Bankers, has suggested that the banks should hold at the Bank of England an hypothecated amount of gold, by means of an issue of 3 per cent. preference gold stock. When we realise that only £24,000,000 of gold is held against £904,000,000 of deposits we can somewhat understand the necessity of an adequate reserve.

CHAPTER XXIII.

THE MANAGEMENT OF DEPOSITS.

THE study of the half-yearly or yearly statements show us somewhat the method how deposits are utilised for the purpose of making a profit on the same. We use the term to include balances on current accounts, which represent capital left by customers in consideration for services rendered, *viz.*, payment and collection of cheques and bills of exchange, also the safe custody of securities and other valuable documents. With regard to deposits it is essential that a higher rate of interest should be earned than what is paid to the depositor.

The management of capital requires great care, not only in order to retain the confidence of the depositor, but especially for the purpose of lending the assets in such a way that no loss shall take place. The confidence of the depositor is somewhat obtained by means of a large paid-up capital contributed by individuals for carrying on the business of banking.

There is also a reserve fund, which consists of profits not divided amongst the shareholders, and also of the premium obtained on the issue of new shares. This fund is kept for the purpose of meeting any extraordinary loss, being also supplementary to the capital account.

The capital and reserve funds of ten London banks are £31,000,000, held against deposits amounting to

£230,000,000 ; the proportion being about 13 per cent. These two assets represent what is considered necessary for the purpose of creating confidence in a business where sudden withdrawals of capital might occur.

The great aim in banking is to keep a proportionate amount of the assets in a liquid form, so that only slight variations should take place.

The first item in a balance sheet is cash at hand, and at the Bank of England ; there must be always sufficient cash to meet any sudden withdrawal ; but no definite amount can be fixed, because what is necessary for a bank in one particular district may not possibly be required in another.

The average cash held by the London banks is about 16 per cent., but this consists of balances at the Bank of England, which have already been discussed.

The next item, " money at call," represents a useful method for utilising surplus funds, since it is essential that no portion of the assets should remain unremunerative. Money at call, however, is not the same as cash, because in times of crisis or panic, bills held as security, or loans advanced against such bills, might not be redeemed. It is, therefore, important that money at call should not be large, or should be considerably less than actual cash, if it is to form part of the cash reserve.

The London banks hold about $14\frac{1}{2}$ per cent. of their resources in this form, but we can at once see the possible effect if £35,000,000 was suddenly withdrawn from the market.

The system of lending money to bill brokers is advantageous to the latter class, since they borrow large sums from the banks at rates which allow a margin of profit on the transaction. Of course, at times the margin is small, so that violent fluctuations in the rate of interest are not desirable. We might illustrate this point as follows :

Suppose money is quoted at 4 to 5 per cent., and the rate for first-class bills is $3\frac{7}{8}$ per cent., if the brokers have considerable sums lent to them at 3 per cent., and they are discounting bills of various grades from $3\frac{3}{4}$ to 4 per cent., there is a margin of profit; if the balance is borrowed at higher rates, there would be a loss.

The method of lending money in this manner is based on the principle that if Bank *A* requires to call money, Bank *B* has a surplus; or if Banks *A*, *B* and *C* require the money lent, there is another group, designated *D*, *E*, *F*, which will make up the deficiency. When, however, all the banks are short of surplus capital, the deficiency is supplied by the Bank of England, which is supposed generally to be in a position to satisfy the requirements of the market.

The system is peculiar to this country, and has many advantages, but, at the same time, requires careful watching. When bills are deposited as cover for loans they become the property of the bank, and if necessary can be negotiated in the usual way.

It is customary to call in loans lent to bill brokers at the end of the month, in order to show a fair cash reserve, and the result is sometimes a temporary disorganisation of the money market. If loans cannot be obtained from the banks, applications are made to the Bank of England, as already explained, in order to restore the equilibrium. The total fund remains the same, but the effect sometimes causes fluctuations in money rates.

Some of the banks do not consider money at call as cash, but include the amount so lent as part of their loans and advances.

Investments form the next item in the balance sheet, and these are of a varied character. It is usual to classify such investments according to their respective values.

The classification would be as follows :—

- (1) Consols and other British Government securities.
- (2) Stocks guaranteed by the British Government, Indian Stocks, Indian Railway Guaranteed Stocks and Debentures.
- (3) British Railway Debenture and Preference Stocks, British Corporation Stocks.
- (4) Colonial and Foreign Government Stocks and Bonds.
- (5) Other investments.

From the above we notice that Consols stand at the head of the list ; it is a recognised custom amongst banks to invest the reserve fund and part of the capital in this security, because of the fact that, in case of need, there is no difficulty in selling large blocks without causing any great fluctuations.

The intrinsic value of Consols is partly due to the credit of the English Government, and also to the fact that the total amount is large. It thus follows that Consols form an important part in our financial system, because it represents part of the reserve fund of banks which have enormous liabilities.

The income derived from such investments is small, but the total amount held has increased in recent years, although there is always an inclination to obtain a higher rate of interest.

It might be said that Stocks in the second and third divisions are equally good, but it is not possible to sell any large amounts, since the market is a limited one, and any endeavour to do so might seriously depreciate the price.

Colonial and foreign Stocks and other investments would be, comparatively speaking, a small amount, the tendency being always to hold only the best class of securities.

The recent legislation by which Colonial Stocks, under

certain restrictions, are allowed to be trust investments will no doubt enhance their value.

With regard to the fluctuations in the prices of Stocks, it must be remembered that a rise in the value of money would lead to the sale of securities, in order to obtain higher rates by discounting bills. Again, large amounts of Stocks are not actually sold on the Stock Exchange, but carried over at various rates of interest, so that when the return on a particular investment is smaller than the interest paid for the loan, the Stock would be sold, and thus cause fluctuations in the price.

The state of trade has also an important effect upon prices, because, when trade is active, the surplus funds of the manufacturer are utilised, and Stocks are sold for the purpose of meeting the increased demand for capital. On the other hand, when trade is depressed and profits small, we find that capital is temporarily invested in securities in order to get a better return.

Another important factor is the state of politics, which at times seriously affect the Stock markets. This is illustrated by the South African War, which has caused a great depreciation in many securities. A banker must, therefore, carefully watch the course of events, so that Stocks, if necessary, can be sold before any great fall takes place.

The market for Consols is always a large one, and the Stock can readily be sold. Although money at call is ranked before Consols, yet in many ways the latter is preferable. For example, if the acceptances of any well-known firm were particularly large, there might be considerable difficulty in obtaining advances on the same.

All the Stocks which are guaranteed by the English Government would be in the same category; Exchequer

Bonds, Exchequer and Treasury Bills are bearer securities, and are held principally by bill brokers.

The London banks hold 18 per cent. of their deposits in securities; the above-mentioned assets, *viz.*, cash, money at call and investments, represent about 50 per cent. of the liabilities to the public.

We have already stated that bills of exchange are an excellent investment, since those documents with several good endorsements may be considered to be the best form of security for a bank's surplus funds. It is usual to divide them into two classes, *viz.*, those which become due within three months, and, secondly, bills of longer dates.

The various rates of interest for bills which are quoted daily in the papers give some idea as to the risks involved in the transactions—the difference between a bank acceptance and that of a small trader being somewhat great. The rule to be observed in all cases is that no bank should hold large amounts accepted by any particular bank or mercantile firm. It is always desirable to minimise the risks by holding bills accepted by many, rather than a small number. With regard to trade bills this rule is usually observed, because a bank would not care to discount many bills accepted by one person.

A bank with a large number of branches is able to ascertain whether the bills discounted are accepted by various persons rather than a few. Thus, if Branch *A* holds bills accepted by *B. & Co.*, and also Branches *B* and *C* hold bills accepted by the same firm, it will be necessary to refuse any more offered for discount. A careful record must be kept of all bills which are discounted for customers, so that the position and standing of each firm whose name appears either as drawer, acceptor or endorser must be obtained.

It is usual to fix a limit as to the amount which the bank will discount for a customer, and this, except under special circumstances, must not be exceeded.

If all the banks separated their bills from the advances, it would enable one to form some idea of the amount held as security, and to ascertain somewhat the amount of trade represented by such documents.

In order to discriminate between *bonâ fide* trade and accommodation bills great care and attention is required; this is one of the risks attached to banking transactions. An account is kept of the standing and position of the various parties to such documents, in order to ascertain the reason why they came into existence.

There are many grades of bills, which is exemplified in the rates of interest charged. For example, three-month bills are discounted, say at rates varying from $1\frac{1}{2}$ to 3 per cent., and we can easily understand the cause of the difference; being, in fact, the degree of risk attached to the transaction.

Bills which are refused by banks are discounted by money lenders at rates varying from 4 to 10 per cent., and this high rate is, in fact, the degree of risk.

With regard to the everyday routine there are two books eminently useful, *viz.*, *The Institute of Banker's Questions on Banking Practice* and Moxon's *English Practical Banking*, which give the necessary information respecting the drawing, accepting and payment of bills, with the laws relating to the same.

A banker should know the practice and methods of different trades, in order to estimate the value of these credit documents. This knowledge can only be obtained by many years of practical experience; the banker must, in fact, know what is going on in everyday life.

Loans and advances form an important item, and re-

quire careful consideration, because many institutions have failed through mistakes having been made in lending capital to unsound borrowers. The history of banking in this country has shown that large advances to any one firm or company has resulted in disaster.

One of the greatest difficulties in practice is to know when advances should be curtailed, or if a loss has been made, to write it off rather than to lend more capital in the hope of recovering what has already been advanced.

A banker is called upon to grant loans on various securities, and we shall briefly consider some of the most important.

BEARER SECURITIES.

This is a class of securities transferable by delivery, and are usually accepted by bankers as security for loans, because there are no formalities required in disposing of the same. These securities form a numerous class, and considerably differ in value; for example, Consol Certificates, Exchequer Bonds and Railway Bonds, guaranteed by the Indian Government, would be readily accepted.

The next class would be Colonial Government Bonds and first-class American Railway Bonds.

Finally, the bonds issued by foreign Governments would form another division and vary considerably in value.

Advances on such securities would be dependent upon their marketable value; the amount of cover required would vary considerably, because a margin of 5 per cent. would be enough in the case of first-class securities, whereas from 10 per cent. to 20 per cent. would be necessary in the case of foreign securities.

STOCKS AND SHARES.

Advances are made upon various stocks and shares, and the same rules with regard to market value and cover would

be applicable to such advances. It is usual to transfer the stock from the registered holder to a nominee of the bank, in order to prevent any possible defect of title. This is done by means of a transfer deed, and as the consideration is nominal, only a 10s. stamp is required.

When, however, the loan is for a short period, a blank executed transfer is accepted, which enables the bank to transfer the stock whenever necessary.

A typical example of a first-class security would be the debenture stocks of our English railways; shares of companies are not accepted when there is any liability, because the bank would become liable for calls made upon the shareholders.

For the same reason advances upon bank shares are not accepted, especially as the liability is in many cases very large. When shares are not quoted on the London or Provincial Stock Exchanges, it is not desirable to advance upon the same. It sometimes happens that the quotation is only nominal, and if an attempt was made to sell a sudden fall in the price would occur. Great care is therefore necessary in accepting such securities as cover for loan.

The shares of many industrial undertakings are really good, but the market being a limited one there is considerable difficulty in selling.

TITLE DEEDS.

Advances made against the deposit of title deeds are not altogether satisfactory, although sometimes it is necessary to grant loans upon such securities. The bank's interest in such property is secured by means of a memorandum of deposit, which forms an equitable mortgage. As a rule, it is necessary for the bank to employ its solicitor in order to

investigate the title, and see whether the deeds are in order.

With regard to value a local land agent may be able to give the necessary information. A second mortgage should not be accepted, since it may happen that when the property is sold there is only enough to pay the first mortgagee.

Advances on house property are not considered good, because there are continual fluctuations in value; the population of a neighbourhood is possibly continually shifting, which consequently affects the selling price of such property. Again, the charges for repairs and increase of local taxation are to be taken into account.

MISCELLANEOUS SECURITIES.

There are some securities which a banker is at times compelled to take, especially when an overdraft has been allowed, and the customer is unable to pay the same. In such case a banker is naturally anxious to obtain some collateral security, and whatever is offered must be accepted in order to minimise the loss which appears inevitable. The customer may offer the policy on his life; when this is accepted notice must be given to the Insurance Company that the bank holds an assignment of the same. If the policy has been some years in existence, and the bonuses are considerable, it is necessary to continue the annual premiums, although for the time being it may show a loss.

Advances upon reversions is another undesirable security, because they are dependent upon the life of another person, consequently no fixed date can be assigned for the repayment of the loan.

Bills of sale form another class which especially should be avoided, since there are so many legal difficulties con-

nected with the same. In order to prevent loans being granted on furniture or stock-in-trade, several laws of a stringent nature have been passed, which, if not complied with, the whole transaction would be invalid.

Again, stock or furniture may be removed without the knowledge of the holder of such bill of sale.

Another undesirable security is that of loans on buildings which contain machinery, since their value is only dependent upon the business in a working condition; so that if the firm or company ceased to exist the selling value would be comparatively very little.

LOANS TO LIMITED COMPANIES.

The growth of joint-stock companies in this country has created another class of securities, which at one time was practically unknown.

The Companies Act of 1900 has been of some value to bankers, because the ability of a company to borrow is practically defined.

The most important point in dealing with limited companies is to see whether they are properly constituted. This is effected by a Memorandum of Association, which must state :—

(1) The name of the proposed company, with the word “ limited ” as the last word in such name.

(2) The part of the United Kingdom in which the registered office of the company is proposed to be situate.

(3) The objects of the company.

(4) A declaration that the liability of members is limited.

(5) The amount of capital with which the company proposes to be registered, divided into shares of a certain fixed amount, and may contain a condition fixing the amount of the minimum subscription on which the directors of the company may proceed to allotment of its shares.

This document, after being stamped, is sent with the Articles of Association to the Registrar of Joint-Stock Companies, and if all the requirements of the Act are complied with, he issues a certificate which is conclusive evidence to the banker that the company is legally formed.

It is important, however, to remember that the company cannot commence business or exercise any borrowing powers unless—

(1) Shares have been allotted to an amount not less than the minimum subscription, and they must be paid for in cash.

(2) The directors must pay for their qualification shares in cash on application allotment, and pay the subsequent calls.

(3) A statutory declaration to this effect must be sent to the Registrar.

If this is in order a Certificate is granted which entitles the company to commence business.

We have, therefore, two most important documents which should be seen by the banker before any business transactions are effected.

A company may obtain loans or advances from a bank by pledging, *viz.* :—

(1) The uncalled capital, or by the issue of debentures.

(2) Creating mortgages.

Sections 14 to 18, relating to mortgages and charges, are perhaps the most important to bankers, they must be of the following description, *viz.* :—

(a) A mortgage or charge for the purpose of securing any issue of debentures.

(b) A mortgage or charge on uncalled capital of the company.

(c) A mortgage or charge created or evidenced by an

instrument which, if executed by an individual, would require registration as a bill of sale.

(d) A floating charge on the undertaking or property of the company.

In order to make such charges valid, they must be registered with the Registrar, and a copy of his certificate must be endorsed on any debentures, if issued by the company.

It is, therefore, important for a banker to see that *every* mortgage or charge which he takes, which “creates or acknowledges a debt,” is registered in accordance with the Act of Parliament.

“The Act does not appear to affect the rights of mortgagees, except by requiring registration as a condition of validity as against creditors and liquidators, and even then subject probably to the exception based on the effect of notice already mentioned. In all other respects the rights of mortgagees will remain governed by the general law.” *

BILLS OF LADING, DOCK WARRANTS AND DELIVERY ORDERS.

In the large seaport towns advances are made against documents representing goods shipped to this country, or after their arrival against documents stating that they have been deposited in a warehouse for safe keeping until actually sold.

A large number of banking transactions are based upon the shipment of goods to and from this country. For the purpose of protecting bankers and others the Factors Act was passed in 1889, which defines clearly the position of an agent.

With regard to such documents a bill of lading may be defined as a receipt for goods embarked, signed on behalf

* Scully, *Lectures on Companies Act*, Ins. Bks., vol. xxii., p. 183.

of the shipowner, undertaking to deliver them at the end of the voyage (subject to conditions mentioned) to a person named, or assigns, or to order or assigns.

The following is a specimen of such a document :—

BILL OF LADING.

Do not deliver documents until draft is paid.

TOPEKA, KANS., U.S.A.,

Nov. 7, 1903.

Exchange for \$200

Against documents attached (Bill of Lading Invoice Insurance Papers) for 500 140 lb. bags of Rocket flour.
B.L. No. 8447. Dated 15.7.03.

Sixty days after sight of this first of Exchange (second unpaid) Pay to the order of The Shawnee State Bank, Topeka, Kansas, Two Hundred Pounds sterling value received, which charge to account of

THOMAS JONES.

To EVANS, JONES & Co.,
London, England.

EXPORT BILL OF LADING.

No. 8847. Lot No. 3090. CONTRACT 864.

FRISCO SYSTEM. ST. LOUIS AND SAN FRANCISCO RAILROAD COMPANY.

In connection with other Carriers on the Route.

Received at Kansas City, Mo., from Thomas Jones, the following property in apparent good order, except as noted (contents and condition of contents of packages unknown), marked, consigned and destined as indicated below :—

Consignee and Destination.	Marks and Numbers.	Articles.
Shipper's order— London, England.	Rocket.	500 140 lb. jute bags of flour. Car. 56,968 C.R.
Party to be notified— Evans, Jones & Co., London, England.		Weight 70,000 lb. subject to correction.

To be carried to the Port of New Orleans, La., and thence by Leyland Line to the Port of London, England (or so near thereto as ship may safely get, with liberty to call at any usual port of call), and to be there delivered as above consigned, or to another carrier on the route to destination if consigned beyond said Port (B), upon payment immediately on discharge of the property of the freight thereon at the rate from Kansas City, Mo., to London, England, of thirty cents United States gold currency per one hundred pounds gross weight and advanced charges , with all other charges and average, without any allowance of credit or discount, one pound sterling to be considered equal to \$4.80 United States gold currency, except that when ocean freight is prepaid \$4.86 United States gold is equivalent to one pound sterling.

Settlement if in currency other than sterling to be at current rates of valuation.

In consideration of the rate of freight herein named, it is hereby stipulated that the service to be performed hereunder shall be subject to the conditions, whether printed or written, herein contained, and said conditions are hereby agreed to by the shipper, and by him accepted for himself and his assigns as just and reasonable.

These conditions, with respect to service before and after delivery, refer to a variety of events which might happen on the voyage, and what risks the carrier will undertake with regard to the said goods.

When bills of lading are received as security, it is necessary to note the arrival of the ship in order to obtain the dock warrants when the goods are warehoused.

A dock warrant is a document issued by a dock company or dock owner, stating that certain goods therein mentioned are deliverable to a person therein named or to his assigns by endorsement.

The following is an example of such a document :—

HAY'S WHARF AND DOCK—BONDED
TEA WAREHOUSE.

3d. Stamp

Dated this 23rd November, 1903.

Warrant for Six Chests of Ceylon Tea entered by
The Proprietors of
Hay's Wharf. } Imported
Declared by the Im- } in the
porter to be Bro- } British
ken Pekoe. } Steamship

SOCOTRA,
Capt. Jones,

From Colombo, and sold by William Evans at
Public Sale, 24th Nov., 1903.

Deliverable to William Evans or assignees by
endorsement hereon,

Subject to the conditions hereon named.

Prompt 26th February, 1904, and all other
charges from the date of this warrant.

Rent commences 27th February, 1904.

OBSERVE.

A weight note for these
goods has been issued, and no
delivery will be made under
this warrant before the ex-
piration of the prompt with-
out the production of such
weight note.

The possessor of the
weight note is entitled to
this warrant upon comply-
ing with the conditions and
sale and paying the balance
of the purchase money, as
expressed on the weight
note, on or before the ex-
piration of the prompt.

After partial deliveries
this warrant will be returned,
and the bearer thereof en-
titled to the remainder of
the teas.

Mark.	Dock Numbers.	Customs Landing Weight.	Customs Tare.	Sale.		Deliveries.			
				Tare.	Draft.				
Kekelwatti	1112	cwt. qrs. lb.	lb.	lb.	lb.				
	3	1 0 19	25	25	1				
	4	1 0 17							
	5	1 0 18							
	6	1 0 19	6 3 24						
	7	1 0 17	Tare 1 1 10						
			5 2 14						

When warrants are issued subject to landing charges, *prime* ones are issued; therefore it is necessary for a bank to have them exchanged for those designated clean, *viz.*, that all charges are paid. The prompt is the limit of time for payment of the purchase money, and this date must be carefully noted. When taken as security such

documents must be endorsed, and all charges for rent liquidated by the customer.

A bill of lading has always been regarded by the law merchant as a document of title, and in some respects superior to a dock warrant.

A delivery order is an order addressed by the owner of the goods to a dock company, warehouse keeper or other bailee, requesting delivery of the goods to a person named in the order.

Banks should not accept a delivery order as security, since it would be easy to issue any number of such documents; actual possession of the goods is necessary before loans are granted.

With regard to advances on produce, a certain knowledge of the markets must be obtained, and to provide against fluctuations in value considerable margins are required.

Another class of loans are designated overdrafts, which mean that the customer is allowed to overdraw his account on payment of interest or commission. This is a distinctive feature of country banking, where a personal knowledge of customers is more obtainable.

Considerable care and attention is required for overdrawn accounts. There are, however, certain rules which should be observed; a careful study of a trader's account will sometimes show whether his business is legitimate or speculative. If a balance sheet is produced showing his assets and liabilities, it is necessary to see whether the former are of a liquid character. For example, land, houses and machinery are sometimes difficult to realise. Again, a balance sheet might be framed in such a manner that it does not exhibit a true statement of the trader's liabilities.

A temporary loan may often be granted without the

slightest risk to the banker ; at the same time care must be taken in order that loans do not become permanent.

We have briefly discussed the most important item in the balance sheet, and it will be seen that the success of a bank mainly depends upon the skilful management of loans and advances.

With regard to liabilities of customers for acceptances, we have already discussed this form of security when treating of bills of exchange.

The result of the management is shown in the profit and loss statement, which exhibits the result obtained by lending the resources.

It has been already stated that gold and notes held in reserve form a contingent fund, so that about 14 per cent. of the assets do not produce any income. The statements issued to the public and shareholders are always in a certain form, and it will be noticed from the specimen balance sheet that the assets are marshalled, *viz.*, they are classified according to their liquid state. For example, cash and money at call would rank before investments and loans.

BALANCE SHEET.

LIABILITIES.		ASSETS.	
	£		£
Capital paid up . . .	1,700,000	Cash in hand and at Bank of England . . .	4,000,000
Reserve fund . . .	850,000	Money at call and at short notice . . .	3,000,000
Deposits and current accounts . . .	17,000,000	Investments—	
Acceptances . . .	2,100,000	Consols . . .	1,300,000
Liabilities by endorsement on foreign bills sold . .	50,000	British Colonial Government and Corporation Stocks . . .	600,000
Other liabilities, being interest due on deposits .	250,000	Other investments . .	200,000
Rebate on bills not due .	16,000	Reserve fund . . .	800,000
Profit and loss—		Bills discounted—	
Balance brought forward .	£ 50,000	(a) Three months and under . . .	3,300,000
Net profit for the half-year .	120,000	(b) Exceeding three months . . .	200,000
	170,000	Loans and advances . .	6,000,000
		Liabilities of customers on acceptances . . .	2,100,000
		Liabilities of customers for endorsements as <i>per contra</i> . . .	50,000
		Bank premises . . .	536,000
		Other assets . . .	50,000
	<u>£22,136,000</u>		<u>£22,136,000</u>

PROFIT AND LOSS ACCOUNT.

	£		£
Interest accrued and paid .	60,000	Balance brought from last account . . .	50,000
Current expenses . . .	20,000	Gross profit for the half-year . . .	259,000
Salaries, rent at head office and branches . . .	80,000		
Rebate on bills not due .	14,000		
Dividend . . .	90,000		
Bank premises account .	5,000		
Balance carried forward .	40,000		
	<u>£309,000</u>		<u>£309,000</u>

CHAPTER XXIV.

BANKS AND THE STOCK EXCHANGE.

WE have seen that the money market is closely allied with the Stock Exchange, and no account of English banking would be complete without reference to the great market for securities.

A century ago the early bankers lent money to the Government; in fact, at that time it was the only outlet for surplus capital. The various issues of Government Stock were then principally taken by the bankers, who agreed to accept a certain rate of interest for the loan of capital.

The buying and selling of Consols created a market which became known as the Stock Exchange. Other foreign countries then found it advantageous to borrow in this country, and the earliest known were Dutch Bonds and French Rentes.

The following is a list of securities quoted in 1850 :—

	£
French Rentes	235,000,000
South Sea Stock	9,554,000
Exchequer Bills	Uncertain
East India Bonds	"
East India Stock	5,000,000
Canadian „	1,500,000
Austrian „	120,000,000

When we compare this with the present nominal value of £8,787,000,000, we can form some idea of the enor-

mous growth of the Stock Exchange. In 1902 no less than £92,000,000 was added to the list, which somewhat illustrates that our country is still the great market for securities.

Every large issue of stock is carried out through the medium of banks; a broker applies for a large amount, and obtains a loan to pay for the same, so that in reality the success of each issue is largely dependent upon our banking institutions.

The system of loans on securities has increased enormously, and on reference to the Clearing House returns for the fortnightly accounts, when stock is either paid for or carried over, some idea is given as to the magnitude of the transactions.

We have on one hand capital deposited in banks, and on the other the Stock Exchange, which is able to absorb such capital in the purchase of securities.

Again, the value of money in the market is to some extent dependent upon the volume of business transacted at that institution; there is, in fact, a close relationship between the short loan market and the value of securities. Whenever there is a rise in the value of money, a corresponding fall takes place in Stock Exchange securities.

It is worthy of notice that the office known as the Rotunda, at the Bank of England, was originally built for, and used by, brokers and jobbers who were dealing in Government Stocks.

The Stock Exchange consists of two classes of members, *viz.*, brokers and jobbers; the former act on behalf of clients, and purchase or sell stocks according to their instructions; whereas the latter deal in the same, and buy or sell to the brokers.

Although London is the great market for the world for securities, there are provincial exchanges at Glasgow,

Liverpool, Manchester and elsewhere, which are utilised principally for the sale of local securities ; or it sometimes happens that if stock cannot be sold in one market, there is a demand at another centre.

Banking is also intimately connected with foreign markets, because there are daily transactions in what is known as International Stocks, which rise or fall in consequence of fluctuations in the foreign exchanges. For example, a broker might find it advantageous to buy in London rather than in Paris, and the difference in price between the two markets would enable the broker to make a profit.

It has been stated that American railway shares were largely introduced on the London market, in consequence of the profit made by what is known as "arbitrage dealers," who buy in New York and sell in London at a profit.

We can see the advantage of being able to find a ready market for the sale of securities, and the jobber or dealer is similar to a merchant who has transactions in other commodities.

What are known as "markets" are groups of jobbers who deal in various securities. For example, we have the American market, principally for American railroad securities ; the Kaffir market, for dealings in South African mining shares. All transactions entered into are for the fortnightly account, and it takes four days to complete the transaction. This is required in consequence of stocks being carried over, which means that, instead of paying for stocks bought or sold, the settlement is deferred for another fortnight on payment of commission, etc. A price is fixed for each stock, and all transactions are based upon the same. This method of business is effected by means of loans obtained from the banks ; we can therefore understand the great importance of studying such fluctuations. It is somewhat difficult to ascertain the

cause of the same, but there are certain known forces at work.

In the first place the state of credit is an important factor ; if trade is active and in a healthy condition, we find greater confidence in the money market, and this indirectly affects values. Profits are being made, and the surplus capital finds its way to the Stock Exchange.

Again, loans granted by banks tend to give an artificial value to some securities ; in fact, borrowed money has an important effect upon the price of all securities.

We know that the prices of commodities rise or fall through the scarcity or otherwise of the circulating medium, and in a similar manner it would affect the price of securities ; if the latter fall more than the former it would mean that there is a general rise in securities. Prices are also affected by the state of politics : the recent South African War was a practical illustration of such effects.

The most important factor is, however, the rate of interest, which naturally more directly concerns the banking community. When the rate of interest charged by the banks is low, we find securities purchased by speculators, who profit by the difference between the rate paid for loans and that which such securities carry.

We have therefore fluctuations in the value of securities due to the rates of interest charged by the banks for the fortnightly account ; if low, speculation becomes active, because stock bought for the rise can be carried over on easy terms, the buyer also profiting by the interest accrued on the stock purchased.

On the other hand, with high carrying over rates the speculator is inclined to sell his stock and close the transaction. It is therefore a matter of great importance to the Stock Exchange as to the charge made by banks for

the fortnightly account, especially as the rates in the house are dependent upon the same.

With regard to the interest charged in the Stock Exchange there are two classes of borrowers, *viz.*, those who obtain their loans from what is known as the money broker, and those who get their accommodation from the banks. It is sometimes advantageous for a broker to obtain his loans without recourse to the banker, because there are less formalities to be observed; naturally, in such cases the broker pays a higher rate of interest.

A quotation from the daily paper shows how the system works :—

Bank rate	3 per cent.
Rates charged by banks and brokers	3 to $3\frac{1}{4}$ per cent.
Rates in the house	$3\frac{1}{2}$ to 4 „

It must be remembered that the money broker guarantees the solvency of the borrower.

The carrying over, or, as it is called, the contango rates, depend upon the nature of the security; thus, at one particular settlement 4 per cent. was charged on American Railway Stocks, and 2s. to 2s. 3d. per cent. on Canadian Railway Shares. At the same time there was a backwardation of $\frac{3}{8}$ to $\frac{7}{16}$ on Brighton Railway Deferred Stock, which is an illustration of a stock being oversold; therefore the buyer, instead of paying interest for carrying over his stock, receives a profit on the transaction.

It must not be forgotten that loans to the Stock Exchange are largely due to speculation; in fact, the greater part of the business is done for those who buy for the rise, and, therefore, do not intend taking up the stocks on Settling Day.

When there is little speculation the rates of interest are low, consequently the loans granted by banks are comparatively small. The contango rates are not only depen-

dent upon the value of money in the market, but also on the amount of speculative business open for the rise; the character of the investment must also be taken into account; for example, in the mining market the rates vary sometimes from 10 per cent. to 12 per cent.

Although such rates are charged on mining shares, the banks only obtained $3\frac{3}{4}$ per cent. to 4 per cent. for their loans to the Stock Exchange.

The speculator's ability to meet losses must also be taken into account, and although he would be unable to obtain a loan from his banker, yet it is possible for him to get the same from a dealer, who, as it were, guarantees his solvency.

The Stock Exchange is utilised by the banks for the purpose of borrowing money on stock; there is, in fact, a close connection between the money and the stock markets. This is illustrated by the price of Consols for money and the account. For example, Consols for cash are quoted $88\frac{1}{8}$, whereas the price for the monthly account may be $88\frac{1}{2}$; the difference of $\frac{3}{8}$ per cent. would represent the value of money in the market. Again, if an investment of £10,000 in Consols is made, it might be advantageous to buy for the account, and utilise the capital sum in the meanwhile at a higher rate of interest.

When money is borrowed on Consols it is not customary to make actual sales, although the contract note might seem to imply such a procedure. A certain amount, including a sufficient margin, is transferred to the lender, and when the loan is liquidated the Consols are transferred back to the borrower. Sometimes this is done by the Bank of England in order to get control of the market, especially when gold is leaving this country, so that the Stock Exchange is indirectly brought into contact with movements of gold to and from this country.

It is a common practice for large undertakings to lend their accumulated earnings prior to being divided amongst shareholders on the Stock Exchange as a temporary investment. This is done through the medium of banks, and the stocks which are deposited as cover for loans are carefully examined.

We have thus given an outline of the connection between banks and the Stock Exchange, and it is of the utmost importance that the system should be carefully studied in all its aspects.

Sir R. Giffen has pointed out the growth of fictitious securities, *viz.*, those quoted on the Stock Exchange, the prices of which do not indicate real values. We can easily understand that price cannot represent actual value if large blocks are pledged to banks, instead of being absorbed by the investing public.

If at any time the banks curtailed their loans, there would be a great fall in prices, and stocks would become unmarketable. We had a practical illustration of this during the crisis of 1890, when Argentine securities could scarcely be sold.

It is therefore essential that banks should not encourage speculation for the purpose of creating fictitious values to securities quoted on the Stock Exchange.

We find every month in the *Bankers' Magazine* a statement as to the price of 325 various representative securities. For example, one month might show an increase in value of £9,000,000, and possibly the next would show a depreciation of £30,000,000. The result seems somewhat startling, but we must recollect that such prices do not represent *bonâ fide* transactions, so there is no actual loss to the banks or their customers.

It is highly important that sufficient cover should be provided on all stocks lodged as security for loan, a margin

of 10 per cent. must in some cases be increased to 20 per cent. in order to provide against contingencies.

The system of loans on the Stock Exchange being transacted through a money broker is in many ways preferable, since he is a better judge of what is really taking place, and able to reject speculative business ; he can also prevent large blocks of any particular stock from being pawned.

Again, the solvency of the borrower is guaranteed by a broker who is able to meet his engagements. We can therefore see the importance of having sufficient cover and the great care required in the management of such business.

We can form some idea of the magnitude of Stock Exchange transactions by reference to the Clearing House returns for the Account and Consols settling days :—

	Account Days.	Consols Settling Days.
	£	£
1890	1,067,400,000	314,800,000
1897	1,113,612,000	362,610,000
1901	1,582,624,000	484,047,000

It speaks well of our modern system of finance when we consider the comparatively small number of failures which occur on the Stock Exchange in proportion to the enormous amount of capital which is transferred on every settling day.

With regard to stocks pledged with banks, it tends to steady prices and prevents violent fluctuations, and thus the intrinsic value of stock is maintained through the action of the banker.

There is also the advantage to the Stock Exchange by means of loans to the dealer, which enables him to absorb large amounts of stock when offered for sale in the market at times when there are no immediate buyers. This prevents Stocks being unduly depressed by sudden sales of

large blocks, and which tends to keep prices at a uniform rate.

No doubt the large growth of deposits in banks has increased the loans on the Stock Exchange, but it is desirable that the business should be kept within certain defined limits.

The banks must also discriminate between securities which are intrinsically sound and those which possess little value. It is also of the utmost importance that fluctuations should be carefully watched; an attempt should be made to ascertain what really are the causes of sudden changes in value.

INSTITUTE OF BANKERS' EXAMINATIONS.

QUESTIONS.—1880.

Give a short sketch of the constitution and special privilege of the Bank of England.

Define a Bill of Lading,

Dock Warrant,

Delivery Order,

and state what are the advantages or disadvantages of each instrument.

What is the difference in effect of an English, Scotch or Irish Bank of Issue establishing an office in London?

1881.

Point out the main characteristics of—

The Bank of England,

The Private Banks,

The Joint-Stock Banks.

What is a Cash Credit?

Is there any limit to the rise and fall of the Exchanges? and, if so, what regulates such limit?

Give some account of the suspension of cash payments by the Bank of England, and the resumption thereof.

Give some account of the crisis of 1857, and the causes that led thereto.

1882.

Give some account of banking in Scotland.

What was the origin of Bills of Exchange?

State generally the conditions under which Banks of Issue are permitted to circulate their notes.

Give some account of the crisis of 1866, and the causes that led thereto.

1883.

Describe the *modus operandi* of the country clearing.

State shortly the leading features of the suspension of cash payments by the Bank of England.

1884.

Give some account of the rise of banking in England.

1893.

Enumerate the various classes of banks in the United Kingdom, and state shortly the nature of their different constitutions.

To what extent are the undermentioned legal tender in England, Scotland and Ireland respectively, *viz.*:—

Notes,
Gold,
Silver,
Bronze.

Give some particulars of the constitution of a Chartered Bank, and define the position and liability of its shareholders.

Do you consider it advantageous or otherwise for a banker to accept bills?

What do you consider the “ liquid resources ” of a bank?

1897.

Explain the meaning and use of the term “ rebate ”.

Describe briefly the method of clearing, and explain its advantages.

Describe the different methods in which a banker employs his resources, placing them in order of their availability in time of need.

What is meant by money at call? Describe the advantage to a banker so employing his funds, and the part such funds play in the money market.

What do you understand by bullion points? Quote the bullion points between London and Berlin.

Give some account of the crisis of 1890, and the means then adopted to avoid panic.

1898.

Quote, as nearly as possible, a recent return of the Bank of England, and explain the different items.

State the usual modes in which a banker employs his resources. Give the usual proportions of each class of assets held by London clearing bankers.

1899.

What are the chief sources of a banker's profit?

Give a short account of the Bank Act of 1844, distinguishing its three principal enactments.

Define the difference between the Scotch and English system of note issue, and state the chief advantage derived by bankers under the former system.

What is meant by "gold points"? Quote the gold points between London and Paris.

1883.

State shortly the leading features of the suspension of cash payments by the Bank of England.

1896.

Explain the term First, Second and Third of Exchange, their object and effect.

State as concisely as possible the relations between a banker and his customer, and those between a banker and the public.

Name five different conditions as to the liability of shareholders under which banks may be formed in the United Kingdom.

What is the effect upon the foreign exchanges of a country resulting from the rise of the rate of interest there?

Compare the position of the Bank of England in its relation to the money market at the beginning of the present reign with that in which it stands now.

Give some account of the circumstances that led to the appointment of the Bullion Committee of 1810.

1901.

Give some account of the various classes of banks existing in the United Kingdom, stating the differences between their constitutions.

Quote, as nearly as possible, a recent return of the Bank of England, and describe the meaning of the various items.

Describe the different methods in which a banker employs his resources, and state roughly the average proportion of each holding that is usually maintained by London bankers.

What is meant by "money at call," and what is the advantage it offers to the banker?

In what way does a rise or fall in the rate of interest affect the rates of exchange?

1903.

State generally the business and duties of a banker.

Enumerate the different classes of banks in England and Wales, stating briefly the differences in their constitution.

Describe fully the different conditions governing the issue of notes in England and Wales by the Bank of England and the Private and Joint-Stock Banks.

Give definitions of the terms Bank Rate, Market Rate, Deposit Rate, Brokers' Call Rate and Rebate Rate. Give some description of the relation between these rates.

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